# Caledonian Trust PLC

**Directors' report and financial statements**
**for the year ended 30 June 2008**

**Company Number 1040126**

# Caledonian Trust PLC

## Contents


| | Page |
|---|---|
| Company information | 1 |
| Chairman’s statement | 2 - 14 |
| Directors’ report | 15 - 17 |
| Statement of directors’ responsibilities | 18 |
| Independent auditors’ report to the members of Caledonian Trust PLC | 19 - 20 |
| Group income statement | 21 |
| Consolidated statement of recognised income and expenditure | 22 |
| Consolidated balance sheet | 23 |
| Consolidated cash flow statement | 24 |
| Notes to the financial statements | 25 - 46 |
| Company balance sheet | 47 |
| Notes to the company financial statements | 48 - 54 |

## Company information

---

| | |
|---|---|
| **Directors** | ID Lowe (Chairman and Chief Executive)<br>MJ Baynham Ll.B. (Hons)<br>AJ Hartley CA<br>RJ Pearson MA, F.R.I.C.S. |
| **Secretary** | MJ Baynham Ll.B. (Hons) |
| **Registered office** | St Ann's Wharf<br>112 Quayside<br>Newcastle Upon Tyne<br>NE99 1SB |
| **Independent auditor** | KPMG Audit Plc<br>Saltire Court<br>20 Castle Terrace<br>Edinburgh<br>EH1 2EG |
| **Nominated Adviser** | Noble & Company Limited<br>76 George Street<br>Edinburgh<br>EH2 3BU |
| **Broker** | Numis Securities Limited<br>10 Paternoster Square<br>London<br>EC4M 7LT |
| **Bankers** | Bank of Scotland<br>Head Office<br>PO Box 5<br>The Mound<br>Edinburgh<br>EH1 1YZ |
| **Registrars** | Equiniti Limited<br>PO Box 28448<br>Finance House<br>Orchard Brae<br>Edinburgh<br>EH4 1WQ |

## Caledonian Trust PLC

# CHAIRMAN'S STATEMENT

### Introduction

This year we report under International Financial Reporting Standards (IFRS's), as opposed to under UK Generally Accepted Accounting Practice as in previous years. The figures for 2007 have been restated to reflect this change.

The Group made a pre-tax loss of £7,875,000 in the year to 30 June 2008 compared with a profit of £398,000 last year. The "operating" loss, excluding property valuation losses was £714,000. The loss per share was 60.25p and the NAV per share was 156.6p compared with 217.1p last year.

Income from rent and service charges was £842,000 compared with £684,085 last year. Gains from the sale of investment properties were nil compared with £16,000 last year. Gains from trading property sales were £105,000 compared with £403,000 last year. Net financing costs were £634,000 compared with £508,000 last year or £310,000 net of the £198,000 net recoverable interest from the Heron Bay development. The weighted average base rate for the year was 5.45% compared to 4.90% last year.

### Review of Activities

The Group's property activities have been concentrated on enhancing the value of our development properties with medium-term prospects, principally by working towards or gaining more valuable planning consents.

The Group's Edinburgh New Town investment portfolio is continuing to change. In Young Street, adjacent to Charlotte Square, the tenants exercised their option to determine the lease in August 2008. We agreed a dilapidations payment and are marketing the property for office or residential use. Residential values of New Town properties are generally higher than office values. Accordingly, we have obtained planning and listed building consent to reconvert the vacant ground and first floors of 61 North Castle Street to residential use and to incorporate the Edwardian extension at the rear of 61 North Castle Street into the contiguous office space in Hill Street. The development margin of the conversion is relatively small and the property is currently being marketed. The adjacent building, 57 North Castle Street, was let to the City of Edinburgh Council with a break option in March 2008 which they exercised. The dilapidations claim is being determined by a third-party expert. 57 North Castle Street, together with 61 North Castle Street, are a particularly elegant pair of Georgian buildings and a residential reconversion is an alternative. In South Charlotte Street the first five-year review of the 4,500 ft² restaurant let to La Tasca for twenty-five years was determined by arbitration at £94,850, a 46% increase!

St Margaret's House, London Road, is our largest property in Edinburgh where we are pursuing different short and long-term objectives. In the short term we seek to stabilise the fabric of the building, to reinstate or repair the services, to defray some of the holding costs and to earn short-term income. To achieve this objective we have let the whole building on concessionary short-term leases to two charities, the English Speaking Union and Save the Odeon Limited, conditional upon repair work that is being undertaken. Occupation of the building has kindled interest amongst other potential occupiers and we are now in discussions with potential tenants for small areas on commercial terms. Concurrently we are pursuing our long-term objective for a large-scale redevelopment. Last year our architects produced an Urban Analysis report covering St Margaret's, the adjacent 125,000ft² Meadowbank House and small varied properties lying between the A1 and "Smokey Brae" which formed the basis for discussions with City of Edinburgh Council. Subsequently we agreed with the Council to produce an overall Development Brief. The Brief is now well advanced, but completion has been delayed due primarily to the very extensive public consultation required by planning policy. The community consultation involved six meetings over three months followed by detailed assessment allowing the Development Brief to be completed shortly which will guide planning and design principles for the redevelopment of the whole area and will constitute a material planning consideration in planning decision and it will form the basis for an outline planning application for the St Margaret's site only. At present four options are under consideration: a residential scheme with 1,500m² of commercial space and either 231 or 258 residential units, or a scheme with an hotel and student residences and 1,500m$^2$ commercial space and either 81 or 133 residential units. Such a redevelopment would have a long lead-in time which, given the current and prospective market conditions, is not inappropriate.

Delays have also affected our large development sites in Waterloo, London and in Belford Road, Edinburgh. Paradoxically these delays have proved advantageous as we have avoided developing during the current deteriorating market. At Waterloo we continue to negotiate with Lambeth Council either to purchase the contiguous site or to enter into an agreement with them to our mutual benefit in order to realise the very considerable marriage value. If the negotiations fail then we will promote a smaller scheme within our site limits.

At Tradeston, Glasgow, on the south side of the Clyde opposite the Broomielaw, we own 100 West Street, currently a purpose-built car showroom let to the Eastern Western Motor Group. The rent review which fell due in May 2006 has recently been settled at £213,000, an uplift of 21.8%. Tradeston was for long considered a 'run-down' area but has recently benefitted from some major developments and the pace of redevelopment has increased recently with the construction of the extension of the M74 through the district to meet the existing M8 at the Kingston Bridge which is due for completion in 2011. We hold a planning consent for a development of 191 flats, predominantly two and three bedroom, together with associated parking and open space and 10,000ft$^2$ of commercial space, but market conditions have not been propitious for this development.

Market conditions have also delayed the start of work on our two development sites in or near Edinburgh. After negotiating for five years we obtained consent for eight houses at a site at Wallyford, which is within 400 yards of the east coast mainline station and near the A1/A720 City Bypass junction, contiguous to development of over 250 houses by two national house builders of which only eleven are still available. In east Edinburgh at Brunstane Farm, adjacent to Brunstane rail station, consents were granted on 13 December 2006 to convert the listed stone-built steading to provide nine houses of various sizes totalling 14,000ft$^2$. Due to market conditions, apart from some necessary demolitions, no building work has started. However, planning proposals to convert an additional stone building to a detached house of 3,500ft$^2$ are well advanced. Adjacent to the steading we own five stone-built, two-storey cottages, a further ruined farm building and two-and-a-half acres of scrubland in the Green Belt fringe adjacent to established residential property. The inclusion of this isolated uncultivated area within the Green Belt is anomalous and we have entered an objection in the current local plan review which is at Public Local Inquiry stage. Any abstraction from the Green Belt would be valuable.

The Group owns fifteen separate rural development opportunities, nine in Perthshire, three in Fife, two in Argyll and Bute and one in East Dunbartonshire. One of these, Carnbo in Perthshire, was acquired in October 2007. Carnbo comprises a five-bedroom farmhouse with over an acre of garden ground within the village settlement and a three acre field just beyond it. Several other properties were appraised, but no further acquisitions were made last year, because the price of suitable rural development properties had risen and the economic outlook had deteriorated.

Many of the opportunities within our rural development portfolio are predicated on a change in central planning policy. In 2005 Scottish Planning Policy 15 paragraph 23 states:- "Opportunities to replace run down housing and steadings with designs using new materials should also be embraced". The rate at which central planning is incorporated into Local Plans varies between Local Authorities. One of the earliest and most significant changes was made by Perth and Kinross Council, where most of our portfolio is situated and to which we have given the earliest attention. The great majority of our portfolio lies in accessible locations set in areas of high amenity. Unsurprisingly, any proposal for change meets local opposition, usually vocal in such desirable areas and, due to the new system of proportional representation, such opposition has more political influence. The process of gaining planning consent is becoming even more tortuous and in some cases the scale of development is being restricted. Paradoxically, the more tortuous the process and the more restricted the permission, the more valuable the consents become - at least in any "normal" market.

The delays in the planning process can be starkly illustrated. In Perthshire plans for four of our five steading developments, which were far advanced last year, have still not been resolved. At Ardonachie Farm steading, near Perth, after extensive and detailed discussions with the planning authority, we submitted a planning application for twelve houses of about 20,000ft$^2$. However, due to policy changes, we have resubmitted an application over £16,429ft$^2$ for ten houses, including a new "farmhouse". At Tomperran, a smallholding near Comrie, where we submitted an application for twelve houses over 19,047ft$^2$, we are required to change the proposed layout again, having previously adjusted it to accommodate a cycle path requested by the Council. The smallholding includes two acres zoned for industrial use and about 34 acres adjacent to the settlement, a proportion of which will be promoted for a housing allocation in the now long-overdue Strathearn Local Plan. At Chance Inn, where we had previously registered an application for seventeen houses plus four affordable houses, we expect to re-apply shortly for a scheme containing ten private houses. At Myreside Farm, in the Carse of Gowrie between Perth and Dundee, we await the decision on the application lodged in September 2007 for eight houses totalling 12,410ft$^2$ on the steading site adjacent to the attractive listed farmhouse.

Planning permission is being sought on three other sites in Perthshire. At Balnaguard, near Strathtay, we have appealed against the refusal of consent for nine detached houses over 15,719ft$^2$; at Strathtay we have just submitted proposals for four large detached houses situated within the village envelope; and at Carnbo we have prepared plans for four houses in part of the former garden ground of the farmhouse.

Planning considerations have also been pivotal in the development of our properties at Gartshore and Ardpatrick. Gartshore lies within a designed landscape with a magnificent Georgian *pigeonnier*, a huge walled garden and a 15,000ft$^2$ Victorian stable block, but, surprisingly, the mainline station near this country property is only seven miles from the centre of Glasgow. Detailed planning studies on possible development have been completed and representations made to the Local Plan. Various consents have been gained at Ardpatrick, a handsome estate looking south east over West Loch Tarbert. However, these are conditional on agreeing servicing and road improvements on both the private and public roads with the Local Authority. The opportunities at Ardpatrick fall into two categories: the first relates to division, restoration and reconstruction of existing properties, residential or otherwise, and the second to "new" houses in areas designated as "Rural Development Opportunities" in the Finalised Local Plan on which the Reporter has recently issued his report. Amongst the Reporter's recommendations was that the "Rural Development Opportunities" should be replaced by other policies. Fortunately the Council have decided not to accept this proposal and are promoting a Post Inquiry Modification retaining the "Rural Development Opportunities", subject to further landscape safeguards. Most of our planned developments in the Rural Development Opportunities will probably meet the proposed tests. Continuing progress is being made in enhancing the value of our properties at Ardpatrick. Many years of neglect have resulted in buildings becoming ruinous, houses falling into some disrepair, ditches and drains becoming blocked, roadways becoming impassable and walls, gates and fences becoming broken or unserviceable, all contributing to a loss of value and amenity and restricting residential and agricultural use. Since purchasing the property seven residential estate houses have been brought back into habitable condition and three outlying cottages sold. A fourth cottage, the Old Post Office, has now been extensively restored and is being marketed. Three outlying buildings whose structural integrity had been impaired have been secured and structural repairs are taking place in Ardpatrick House and essential repairs are taking place to roads, ditches and drains, to restore the agricultural value of the property, to improve amenity and to allow the for enhancement of the sporting potential.

Agricultural values have risen, often considerably, in all our farming properties. We judged that as these are ancillary to our main interests, that as prices had risen considerably and that as the capital could be more profitably deployed elsewhere we should realise them and we have been marketing our farming land at Larennie in Fife, where we will retain the buildings and prospective development land, and at Chance Inn, near Kinross, where we retain the farmhouse, development land and steadings. Interest has been considerable and this arable land is all "under offer" at attractive prices. The land at Ardpatrick, none of which is arable and where the marriage value with the Estate is considerable, is currently being retained and its utility improved.

**Economic Prospects**

In 1808, two centuries ago, The Reverend Dr Robert Walker died. Raeburn's portrait of him, "Skating on Duddingston Loch", is one of Scotland's most famous. Until last year economic and skating analyses were analogous - the prospects for the ice, that is the economy, its condition, its thickness or thinness, its growth and the risks to that growth, and, as described by Lord Cockburn "the poetry of motion" of Dr Walker's exquisitely elegant pose", "the travelling position", requiring "diligent practice and considerable sophistication". Analogous perhaps to the prudent pose of the accelerating travelling of the UK economy, skating through 63 quarters of uninterrupted growth under the diligent and sophisticated hand of the newly liberated MPC, one of a trio of regulators, evocative of the Trinity overseeing the Reverend Doctor.

In years of "steady skating", analysis was of the conventional business cycle fluctuating around a trend of rising output based on the growth capacity of the economy adjusted for budget deficits, fiscal prudence and the possibility of outside shocks, particularly through oil prices, as had occurred before, or the faint possibility of a collapse in the faraway USA housing market. Risks to the world economy appeared manageable: oil's importance in relation to output had fallen and the risk of a housing market collapse was minimised as a serious threat because it was a sector responding to low interest rates, and because numerous commentators had cried "wolf" before. Even this year as the present crisis unfolded the banks stated they were well funded, indeed as the Chairman said " allow us to continue on the impressive growth trajectory that has characterised RBS …" patently few knew how thin the ice was on which they skated. However, following the initial failure, fractures have radiated and propagated in every direction carrying all the skaters into the deep cold. Samuel Brittan describes these fractures as "apocalyptic", "threatening the very existence of the world monetary systems" and creating a new game where the cliché about "the old rules no longer applying" is for once correct. The relevant analysis now is not about the state of the ice or the fluctuations of the economy about trend, but about how deep and cold the water will be, how long and how deep the UK recession will be and what can and will be changed to get the maximum number of survivors to the shore.

On 6 November 2008 the MPC cut the repo rate by 1.5 percentage points, a cut three times larger than any since the MPC was established in 1997, to 3%, the lowest rate for 54 years. The MPC explained that there was "evidence of a severe contraction in the economy……, and such a dramatic extinction of inflationary pressure that at prevailing rates there is a substantial risk of undershooting the inflation target". Previously the MPC has been restrained from larger cuts because of the threat of increased inflation, an opinion not widely shared, which, according to many economists has resulted in an overdue delay in cutting interest rates. Indeed some economists judged that the 1.50 percentage point cut is "barely adequate and will probably need to be followed by further cuts soon". Martin Wolf, writing in the FT following the November cut, says "the risks of doing too little are far greater than those of doing too much: sometimes boldness is caution". Since the November cut there has been what the FT cites as a "further sudden and brutal deterioration in the economic outlook" and on 4 December 2008 the MPC cut the repo rate again, by 1 percentage point on this occasion to 2% equal to, the lowest rate since the Bank of England was founded in 1694. Contemporary cuts were made by the ECB to 2.5%, the Fed to 1% and the Bank of Japan to 0.3% and since then the Fed and the B of J have made further cuts to 0.0 to 0.25% and 0.1% respectively. Some commentators still judge the B of E's and the ECB's "measured step-by-step approach" to be an inadequate response when extreme measures similar to the Fed's are necessary.

Unfortunately, the effects of the cuts in interest rates may be attenuated. Borrowers are unlikely to obtain a full reduction in rates as the banks' costs are not mechanically linked to official rates but have a high marginal and a rising average cost of capital due to expensive equity, including preference stock, and increased margins over base rate on their inter-bank borrowings. Cheaper money makes spending, including that funded by borrowing, more attractive relative to saving, but the availability of the desired borrowing at "normal" prices may be curtailed as the banks reduce their loans in order to improve their capital ratios. In the past few years the banks increased their external funding to increase turnover and profits, giving lower capital ratios, but recently have suffered substantial equity losses further reducing their capital ratios. Only seven years ago Britain's banks funded lending almost entirely out of customer deposits but by 2008 the funding gap, met by international wholesale money markets, was £740bn. The scale of the total Bank equity losses since early 2007 is estimated by the Bank at £1,700bn equivalent to 85% of the banks' Tier 1 Capital. British banks will have at least a proportionate share of these losses and Morgan Stanley report that European banks alone will need a further £67bn of equity, having already received £94bn this year alone. The total of the rescue plans, - including capital injections, taxpayers' support and government guarantees on wholesale funding - made over the summer, culminating in the US TARP crisis in early October, for the ten largest recipients was an astonishing $3,390bn.

The rescuers have two objectives. The first is to "see off" systemic risk ie the collapse of the banking system and in its wake the whole financial system. The cost of such a collapse was recognised as so immeasurably high and so immediate that all administrations affected set aside all moral, political, administrative and ideological considerations to save the system. The Economist put it "deft policy saw off calamity". The second objective is damage limitation: to minimise one or more of recession, depression or deflation. Fiscal policy is within the control of the Government and measures to stimulate the economy, including the VAT rate reduction, have been announced. Discretion is wide but subject to economic sanction though a collapse in Sterling and from increased borrowing costs, if measures are considered "extreme". However, many Eurozone countries have net debt above 50% of GDP and historically the UK has prospered in spite of increasing debt. Harold MacMillan in his only budget speech noted that debt had risen from £600m in 1914, to £8.4bn in 1939, and to £27bn in 1956 - 27, 133 and 146% respectively of GDP. He put it so: "whatever the temporary difficulties of trying to run too fast, if we stood still, we are lost."

Monetary policy, subject to Government control over inflation targets, is determined by the MPC except insofar as the inflationary target jeopardises "economic stability". Deflation, not inflation, represents the major risk to the MPC's target and monetary policy will be very expansionary. Policy changes do not act directly on the "real" economy but are intermediated via the banking system where the present unusual circumstances limit their efficacy. The higher cost of bank capital referred to above restricts the transmission of lower interest rates to the real economy. However the main restriction is the banks' requirement to improve capital ratios which will be damaged further by increasing write-offs from the gathering recession. Reducing lending would improve ratios more rapidly, but this is contrary to the Government's stated policy that the banks' bailout is conditional on returning to 2007 levels of lending. Thus the Government's objectives, improving capital ratios and maintaining lending, are mutually exclusive - an unfortunate dilemma.

Another dilemma faced by the banks is described by J M Keynes as the "Paradox of Thrift", in which if each bank does what is prudent for itself, by cutting lending, then such action slows the whole economy and further hurts everyone, including itself. Changes in bank lending have a multiplier effect on the economy, so elegantly simplified as a "game" with his students by Harvard Professor Niall Ferguson. In the game he deposits a $100 Government fee with Student Bank A which deposits $10, the necessary 10% reserve, with the central bank and lends $90 which is deposited in Student Bank B which deposits $9, the 10% reserve, and lends $81. After three rounds the total money is $271 and after an infinite number the sum is $1,000. Then Professor Ferguson springs a surprise on Student

Bank A, by asking for his ($100) deposit money back. The process then has to be unravelled and the banking system shrinks not just by the original $100 deposit but by $271, if it has "gone" three rounds. Reductions in credit have a snowball effect on the economy and hence the Government's concern.

Deft policy has indeed "seen off" calamity, but how did the impending calamity arise? Or, as HM the Queen disingenuously enquired of the Director of the London School of Economics Professor Luis Garicano, "If these things were so large how come everyone missed them?". Patently, as the FT surmises, the Queen had not been briefed "from the man who comes weekly to tell her what is going on - not the nice smooth one - he went some time ago. Now it's the grumpy Scottish one" whose view is that the crisis materialised unannounced as an evil spectre fleeing New York. Professor Garicano reportedly replied that "at every stage someone was relying on somebody else and everyone thought they were doing the right thing". In practice it seems that house buyers bought because, if someone was prepared to lend the money, then it would be ok, lenders reckoned if they securitised the loans they would be ok, financial institutions thought that if the credit rating agencies gave approval they would be ok and the credit agencies thought - so finessing any cerebral activity - that whatever everyone else was doing they better do too and the regulators didn't know, didn't want to know and, if they did know, they certainly did not wish to understand.

However wrong the regulators were, their behaviour was neither random nor inexplicable. Over the past generation the financial system has changed from regulation to de-regulation and the intellectual climate in the Anglo Saxon economies turned in favour of the primacy of the markets and against regulation, a change eventually and reluctantly followed by continental Europe and by Japan. The success of the market economy, latterly including sophisticated financial engineering, facilitated and reinforced by the flood of cheap money from Asia and oil producers' savings, powered the considerable expansion in the world economy. It is self-evident that, given the exceptional returns, there was no potential incentive to question too deeply their origins or dependability. The permissive changes resulted from a combined series of alterations in organisation, procedure, methodology and culture which did not change with a "jump", a saltation in evolutionary terms, but by a gradual process of evolution ultimately yielding the entirely new deregulated "species".

Deregulation has its origins in 1971 when the post-World War Two Bretton Woods system of fixed exchange rates and the convertibility of the dollar to gold were suspended and currencies "floated" like commodities. Agricultural commodities and their derivatives had been traded for over 100 years in Chicago, the "market" town and shipping centre for US agriculture where in 1972 Leo Melamed, chairman of the Mercantile Exchange, launched futures trading also in currencies, an innovation that extended to Treasury Bills in 1976, Eurodollars in 1981 and stock index futures in 1982 and founded today's varied and complex financial derivatives. Agricultural pricing starkly demonstrates the laws of supply and demand and the clear effects of competition. Such an environment was conducive not only to the transfer of the principle of trading commodity derivatives to trading financial derivatives but also the transfer of the principle of free agricultural markets to free market economics, an intellectual position promoted by the Chicago School headed by the monetarist, Milton Freidman, who argued that markets allocated resources more advantageously than policies more inclined to Keynesian principles which placed more emphasis on central control and allocation.

The intellectual arguments were reinforced by political power when the severe recessions of the 1970s led to the election of the conservative free marketeers, Margaret Thatcher in the UK and Ronald Reagan in the USA. Credit controls were soon abolished and institutional changes made to give easier access to credit, particularly house mortgage credit, a change designed to assist the political ambition of more widespread house ownership, and other liberations followed, including the abolition of exchange controls. Growth, liberation, cross border investment and mergers and acquisitions led to a quantum increase in currencies, money and shares traded and handled largely by a long-established cartel of wholesalers, jobbers, and brokers. Cartelisation reduced competition and the small scale and capital base of most operators hindered large transactions and increased their cost. This structure was swept aside by "Big Bang" in 1986, a similar reform having been carried out in New York a decade earlier.

Big Bang reverberated widely. Competition forced down commissions and higher turnover increased capital requirements - brokers, jobbers, banks and merchant banks aggregated in various combinations to benefit from vertical integration and to use their own capital to finance deals as well as broker or advise on them. In the USA the two activities, merchant/investment banking and commercial banking, were strictly segregated by the Glass Steagall Act, but the distinction became increasingly attenuated until its repeal in 1995. In both the UK and the USA investment houses wanted to be banks to trade on their own behalf, while commercial banks wanted to become investment banks to gain access to high professional and agency fees. From the mid-1980s in the USA and the late 1980s in the UK both economies moved to a low inflation rate and asset prices, bonds, property and equities, rose for most of the subsequent periods (except for short recessions), producing a boom in lending in and against all these asset classes for the liberated commercial banks and the diversified investment banks. The US financial sector rose form 8% of total stock market capitalisation in 1984 to 24% in 2007.

The discovery of a theory of option pricing by two Chicago School economists, Fisher Black and Mervyn Scholes, based on the volatility of the underlying asset, facilitated a further expansion of tradable derivatives. Futures derivatives originally based on agricultural commodities, were joined by options priced through the mathematical formula of Black Scholes and then by swaps, initially between currencies, then between fixed and floating interest rates, and then by credit default swaps, CDS, which in 2008 had $60tr outstanding. Derivatives all share two important characteristics: by definition they are "derived" and in practice they are very highly geared as a small initial equity position, which itself may be geared, gives access to, or responsibility for, a very much larger position. These potentially huge positions change rapidly and, although real risk remained, they were effectively off the balance sheet. Thus they are not easily regulated.

Securitisation, another means of gearing up, often off the balance sheet, originated in the 1970s, but was exploited principally from the mid-1990s, added very considerably to the complexity of the banks' operation, and their regulation. It allowed the banks to sell the cash stream from their mortgagors, keeping the fees and usually some continuing income stream. Asset-backed securities in the USA grew from £300bn in 1995 to £2,500bn in 2007 due to securitisation's magnificent attractions: risk was spread, banks earned fees without encumbering their balance sheets and investors got higher yields from diversified mortgage payers backed by secure assets than they paid on mainly short-term borrowings. A grave weakness of the system was that the originators were rewarded by immediate fees and volumes whereas the purchasers were rewarded by the long-term cash stream from payers of uncertain creditworthiness and asset value: hardly parallel objectives. Professor Ferguson, referring to the $120m losses of three municipalities in the Arctic Circle, encapsulates an extreme position: sub prime mortgages of 100% LTV could be arranged on day one in Detroit, a notorious centre for the scam, 100% NINJA (No Income No Job or Assets) mortgages packaged on day two as CDOs, sold to another bank or intermediary and in no time at all the risk was floating up a Norwegian fjord!

Until the credit crunch deregulation, reliance on market forces and financial engineering appeared beneficial facilitating cheaper and more accessible credit, higher home ownership, higher consumption and higher profits and universally rising asset prices. Little wonder no one tampered with this goose, a particularly fecund and fickle one, whose golden eggs came from a nest of intricate and elaborate camouflage. Equally sacrosanct was the plentiful and nourishing elixir fed to this goose, a steady stream of savings produced, surprisingly, a long way away in China. In 2005 Chinese savings were 45% of Gross National Income - in the USA they were under 2% - of which a large portion flooded into the USA and this supply of savings resulted in global real interest rates falling to 67% of their previous fifteen-year average. While cheap credit was of great benefit it also provided the feed-stock on which financial engineering flourished, a success story as inscrutable as its oriental association and one certainly unscrutinised - to our present great distress. The subsequent losses in financial markets are prodigious. The Bank's currently misnamed Financial Stability Report estimates that UK losses since 1 January 2007 on securitised credit investments and corporate bonds are £1,700bn, more than the UK's annual GDP or 85% of the bank's Tier 1 capital before the crisis.

Britain, the USA, the Euro zone and Japan are already in a recession that for some threatens to be the worst for a quarter of a century and possibly since the Depression. How bad will the recession be? On 16 October 1929 Professor Irving Fischer of Yale University declared that US stocks had "reached what looks like a permanently high plateau", but by 29 October the market had fallen by 25% and over three years lost 89% of its value. The US Stockmarket crash that turned into the Great US Depression lasted four years in which GDP and employment fell 30%. The crash was preceded by a "bubble" in stockmarket prices with hi-tech stocks like RCA rising nearly 1000% to a PE of 73. A credit boom fuelled the rise in stock prices, often bought on margin, a leverage similar to the use of derivatives now, and the boom facilitated a rise in consumption, based on instalment credit, and a fall in savings, all eerily similar to the current rise in debt-based consumption.

In 1963 Milton Friedman argued that the Federal Reserve System bore the primary responsibility for turning the crisis of 1929 into the Great Depression as it did not expand credit and at times caused its contraction. Prior to the crash a small number of banks had suspended payments and this growing tendency reached a critical mass in 1930 when 608 banks failed with losses of $550m ($6.8bn now, inflated by the CPI) of which nearly $200m related to the large Bank of United States whose possible merger with a "white knight" the Fed failed to secure. In the following credit contraction the Fed permitted banks to sell assets and bonds for gold further restricting credit and increasing bond yields and interest rates. Bond yields were increased again when the UK abandoned the gold standard in 1931 and the Fed raised the discount rate to prevent a $ depreciation. Finally, expecting a $ devaluation from the Roosevelt administration in 1933 that was famously later to promote a "New Deal", the Fed once again raised the discount rate. Two days after his inauguration on 4 March 1933 Roosevelt proclaimed a nationwide bank holiday from which 2,000 banks never returned. Due to the credit contraction about 10,000 banks failed and, although surviving banks increased their reserves, commercial banks decreased deposits by 37% and loans by 47%. In this great contraction public cash increased by $1.2bn but bank deposits decreased by $15.6bn and loans by $19.6bn, equivalent to 19% of GDP. The lessons of the great crash are, firstly, that, following a sharp decline in asset values, unless monetary policies are permissive with low interest rates and supporting credit, a correction can gradually fall into a recession and a recession into a depression and, secondly, that the benefits of exchange rate stability do not outweigh the benefits of avoiding deflation.

Analysis of the great crash shows that the Bank of England's reaction is the crucial variable in determining the extent of the current UK recession. The scene was set early when there was a run on Northern Rock and a proposal to link it with Lloyds TSB was not supported and the Bank seemed to be preoccupied with moral hazard, or, more generously, with the study of conflagration rather than the suppression of the engulfing flames. As recently as August 2008 escalating inflation was identified as the key risk and economic output was projected to be "flat", but in that quarter the UK entered recession with interest rates at 5%. By November 2008 the greater concern was deflation and the Bank then forecast a peak-to-trough decline in GDP of about 1.9% with the recession lasting into late 2009. In another volte face the Governor reversed his opposition to a fiscal stimulus, saying the "transmission mechanism" of monetary policy had become impaired through the banking crisis. In accordance with this damascene change the Bank cut interest rates to 3% in November, and stressed that fiscal policy was likely to be relaxed and that MPC would be able to take further action to lower interest rates in the months to come, a commitment delivered by the cut to 2% in December, equal to the lowest level since 1694. By way of some reassurance the Governor said the expected recession would not be like Japan's "lost decade", 1996 to 2005, and milder like Sweden's in the early 1990s: a recession that lasted from 1990 to 1993 with a contraction of almost 5%. At least he did not compare it to the great US depression.

Contractions in economic growth have occurred in every decade since World War One. A vast inflation followed the First World War succeeded by a savage deflation. The 1920s, including 1926, the year of the General Strike, brought a 4½% contraction and the 5% recession in 1930 occurred as the Sterling left the gold standard. After World War Two contractions of up to 6% occurred in each year from 1944 to 1947, and there were small recessions in the late 1950s and early 1960s. The recessions in 1973-74 and 1980-81, both lasting about six quarters, related to the shocks delivered to the world economy by the very rapid increase in oil prices and the economy contracted 3.5% and 6.1% respectively from peak to trough. The most recent recession in 1990-91, following the stock market crash of 1987 and the high inflation of the late 1980s, saw a peak to trough fall of 2.5%.

Forecasts for the UK recession have been getting steadily more pessimistic. In October the IMF predicted GDP would fall 0.1% in 2009, but in early November the European Commission predicted a 1% fall, the biggest drop amongst the 15 "old" states in the EU. The Economist poll of forecasters in October predicted 0.1% growth in 2009 but revised it to a 0.1% contraction in November. Currently even the Bank has moved from "flat" in August to -1.9% in the November report. The CBI forecast a peak to trough of 2.5% with the trough occurring late in 2009.

There is no common cause of recessions over the decades, but re-occurring themes have been wars, external shocks, particularly oil prices, asset booms - finance, property, commercial and domestic, and stocks - and inflation. The current recession is clearly not as a result of conflict, nor an external shock from a sudden sustained rise in oil price. Nor is it a result of inflation, which at its recent peak was well below that in earlier episodes and was principally related to short-term rises in food and energy prices. Nor does it seem directly related to stock exchange or equity over-pricing, unlike the 1920s or even the dot-com boom: the main underlying cause is related to credit. Asset prices rose as a result of the huge credit surpluses recycled to the Western economies whose distribution was facilitated by benign and largely unregulated intermediaries, including principally what were regarded as the most sophisticated banking systems the world has known. This credit bubble burst as it was discovered the assets were not there, "the emperor had no house" and the contraction of credit, due to solvency and liquidity, and liquidity and solvency, each reinforcing the other, is resulting in the current huge contraction. Failing a direct comparison the current recession is nearer in cause to that of the 1920s than to any other decade. Fortunately, this view is now being embraced by both the monetary and fiscal authorities and the mistakes of the 1930s are not now being repeated. However, with a different cause than recent recessions, it is misplaced to gauge the length and depth of the current recession by reference to them. Capital Economics state "this is the worst financial crisis since the 1930s" and forecast a further contraction of over 3.5%. In view of the unique cause of this, downturn, of the continuing deterioration of the survey results and of their progressive downgrading by subsequent forecasts, I consider that the outturn will be towards the worst levels forecast.

**Property Prospects**

The CBRE All Property Yield Index fell steadily from a peak of 7.4% in November 2001 to a trough of 4.8% in May 2007, was 5.1% in August 2007 and has continued to rise each quarter to reach 6.5% in August 2008. If there had been no other change in the last fifteen months, then the value of the underlying property would have fallen 26.2%.

In August The All Property yield of 6.5% was two percentage points higher than Gilts but is now three percentage points higher than the current Gilts yield. In May 2007, with property yields at their recent low of 4.8%, they were 0.6% points below Gilts - a "reverse yield" gap of 0.6%. The All Property Rent Index fell 0.8% in the quarter to August 08, primarily as a result of a 2.2% fall in Office rents, where Docklands and City rents fell 5.9% and 4.0% respectively, and 0.1% in the year to August 2008 when Docklands and City rents fell 12.2% and 9.7%.

Unsurprisingly returns to property investment have been truly awful. In the year to 30 September 2008 the IPD All Property Index returned minus 18.1%, only marginally better than equities, minus 22.3%, but the 5-15 year Gilts Index returned plus 8.8%. The fall in the IPD Index in September was 2.4%, but this was exceeded in October by an even larger fall of 3.8%. The Total return in the IPD twelve month rolling index has fallen every month for the last twelve months from 5% in 2007 to the minus -24.5% in October 2008. Over the same period projections of future returns, as measured by the IPF forecast survey, have also continued to fall. In October 2007 the All Property returns were forecast as 2008 0.9%; 2009 5.7%; and 2007-11 4.9%; but the current November 2008 forecasts are 2008-16.8%;

2009 -5.3%; 2010 +6.2% and 2008-12 1.7%. The forecasts made by Cluttons and Colliers CRE both exhibit the same pattern of losses in 2008 and 2009 but return to profit in 2010. All forecasters expect the office sector to be the worst performing, particularly London's West End and City offices, where IPF forecast a 15.4% loss in 2009.

The IPD All Property Index forms the basis for "swaps". Over the year the estimated future returns based on this swap have also declined markedly and currently show negative returns until 2010 (-1.71%). The swaps market indicated the extent of the current downturn more quickly than other surveys and forecasts but, as the Tullett Prebon November review says, "At such times, derivatives markets often over-shoot the underlying market …. and it could be argued that such a situation exists now in property ... ". Currently the swaps market implies a peak-to-trough capital return of over -50% and yields of 9.0%.

Last year I expected yields to rise to 6.50%± 0.50% and obligingly the CBRE All Property average yield in August 2008 was 6.50%! Previous property "crashes" occurred between 1972 and 1974 and between 1988 and 1991 when yields peaked at 8.7% and 8.6% respectively, 2.7% points and 2.2% points higher than the lows immediately preceding them, implying a fall in property values of 31.0% and 25.6% respectively. If the past yield rises, 2.7 and 2.2% points, are applied in the current downturn, yields would rise to 7.5% or 7.0% respectively. Conversely, if past falls in property values of 31.0% and 25.6% occurred from a current "low" of 4.8%, yields would rise to 6.95% and 6.45% respectively. Patently 6.45% is too low an estimate, having already been exceeded.

The property crashes of the early 1970s and the late 1980s were primarily the result of, but not the cause of, these severe economic dislocations. The present position is antithetical as property, primarily the loss in value of residential property, has precipitated the severe dislocation. The two previous dislocations occurred during times of high inflation (12.5% and 6.5%) and high interest rates and were triggered by the oil shock or by exchange rate difficulties. Currently inflation is low, there is no oil shock - and the fall in Sterling, assisting exports and import substitution, is probably very favourable, given low commodity prices. This recession is characterised by low inflation and by a threat of deflation. Repo rate is now 2% and, based on BBA REPO forward rates will average *c*1.50% in 2009, and future markets are pricing a 1.4% point fall in Libor rates by September 2009. Such low interest rates should provide excellent returns on well let investment property. For illustrative purposes say interest margins rise to 175 basis points, LTV falls to 65% and Libor rates are 3.0% (repo rate is ≤ 2%) and investment yields rise to 7% from the current 6.5%, then on these assumptions income return to equity is 11.2%, probably about 10% in real terms with excellent prospects of capital growth. Unless the forthcoming recession is similar to those occurring in the post-war periods or in the 1920s, I think the persistence of investment yields above 7.0% is very unlikely.

"Is this the end of the house price boom?" - so John Kay wrote in the FT as long ago as 12 October 2004. He carefully distinguished the house price boom from bubbles such as dotcom stocks, Victorian Railways, the South Sea Company and the tulip mania of the 1630s. He asserts that the "assets" in bubbles have little or no intrinsic value except to those whose beliefs are similar to the mass hysteria that led people in the 17th Century to believe in witches or in the 21st Century in abduction by aliens. His conclusions were: that housing is a good long-term investment, that the current boom will be followed by a sharp slump (as now!), and that those who make "confident" predictions about the future of house prices are mistaken!

Last year I reported that in November 2007 there had been several indications of house price instability. In fact the market had peaked in August 2007 and as the position was succinctly put then by Academetrics "the expectation for a slowing market ……remains regardless of any decisions by the Bank of England. Indeed, the Bank's previous increases have now collided with the tightening in mortgage credit resulting from the sharp increase in mortgage arrears and repossessions and loss of confidence in mortgage-backed securities in the US market and, to a lesser extent, in the UK".

Since November 2007 both the Halifax and Nationwide report price falls of nearly 15% and the Halifax an 18% fall from the August 2007 peak. Year-on-year falls of 10.1% are reported by the Land Registry, 8.2% by FT HPI, and 6.3% by Rightmove, all lower than the two mortgage lenders probably due to delays in reporting and to differing mixes of properties. Some new builds are allegedly available at over 20% off "new" prices and bulk new builds are reportedly available at up to 40% off, while repossessions generally sell for at least 10% - 30% below discounted prices.

Forecasts of prices cover a wide range. The Treasury, expect at least a 25% peak-to-trough fall before a "recovery" in 2010 and the Halifax and the Nationwide both estimate the overall fall as 25%. The Centre for Economies and Business Research made a similar forecast in October and expects prices to rise "20% through 2011and 2012 as fundamentals reassert themselves" and nearly to regain 2007 price levels. JLL forecast a peak-to-trough fall of about 29% with a delay in the recovery of 2007 prices until 2010. Roger Bootle of Capital Economics forecasts that the 15% fall reported in October "is just the start and that prices will eventually drop by 35%". However the most pessimistic forecast is derived from the Property Derivatives based on the HPI. In May 2008 the contracts implied falls of 12.0%, 8.5% and 6.3% over three years and with small falls extending to 2015, but by November 2008 the corresponding figures were for falls but for three years only of 22.0%, 14.0% and 3.0%. The market makers comment that "Instinct suggests that these prices are too low …. liquidity is an issue in this market due to lack of buyers with prices potentially being pushed to artificially low levels … these longer dates contracts appear to offer an excellent opportunity and a large discount". The FT comments that house price derivatives markets are not the perfect guide to the real thing as they are often illiquid and dominated by mortgage banks seeking to hedge their mortgage exposure.

Other indicators used to estimate future prices include the ratio of the price of houses to earnings of which the long-term average is four. In November 2008 the Halifax average price was £163,605 and earnings were £35,878, a p/e of 4.56. Given constant earnings house prices would have to fall to £143,513, or a further 12.3%, to reach the long-term p/e of four, a fall of 28.1% from the August 2007 £199,600 peak. Another commonly-quoted yardstick is "affordability" - initial mortgage interest and capital payments as a percentage of "take-home" pay. Current payments at 45% are above the long-term average and house prices, *ceteris paribus*, would have to fall a further 18% or 33% from the peak to bring payments back to the long-term average of 37%.

The array of derivatives, benchmarks, historical patterns, trends, estimates and forecasts allows the comfort of "authority" for varied predictions but little causal basis for them. The availability of credit is a major factor influencing the housing market, the current rationing is due to bank losses restricting lending, and the consequent questionable solvency of some banks reducing their trustworthiness or creditworthiness (from *credere* to trust) so that funds normally available between institutions are reduced, further restricting lending. The housing market, being more dependent on credit than virtually any other sector, will continue to have demand curtailed until "normal" credit is restored. Fortunately, showing excellent judgement, the authorities led by the USA, which did not share the Bank of England's damaging initial reluctance, have first saved the banking system and are now using the necessary extreme measures to ease credit supply which in time will reflate the market.

Another factor strongly influencing prices is that the housing market is not a "random walk" i.e. where prices are as likely to be down as up. The reverse is the case: if house prices rose last year, there is strong evidence that they rise this year - price series display positive serial correlation in the short term: house prices have risen because they have risen. However, price series show negative serial correlation in the long term, or, a period of several years in which prices rise by more than the average, is generally followed by a period of similar length in which prices either fall or rise by less than the average. The overlying credit shortage has concertinaed this affect producing rapid falls which are self-reinforcing. When the market becomes more active and the expectation of further falls becomes replaced by an expectation of further rises, then the current serial pattern will reverse again.

These two factors are subsidiary to the main underlying influences which they modulate, the supply and demand for housing, the ultimate determinants of price. The supply of houses is relatively inelastic and slow to respond to changes in demand. The supply is limited by the long cycle time of acquiring, planning and then producing. The supply is further restrained by the planning process which determines how many houses shall be built in a given place in a given time but then, because of increasing complexities in the planning system, is frequently unable to deliver the programmed number of houses. Within established housing areas supply is even more restricted, especially where listing or conservation restrictions apply. Demand is much more variable, especially in the short term. As noted credit supply is a major determinant of demand and at present a major inhibitor of it, especially as the option to defer a purchase is usually available at least in the short term. However the costs and inconvenience of delay over a longer period increase rapidly, so demand is only deferred, and the underlying demand for houses, according to the currently used econometric models, is likely to keep growing. Thus the housing market presents a paradox. In the long term there is a fundamental imbalance between a supply which is subject to considerable restriction and a requirement, measured according to various models, which is greater than has normally been available. Both the long-term supply and the demand parameters may not be unaffected by the present severe recession, but I expect any such change to leave the fundamental position intact. However, in the short term the reverse is the case: the demand is so curtailed that supply, so restricted in the long term, is in surplus in the short term.

The key question for the housing market is how long is the short term? Fortunately the major cataclysms have been avoided. The threatened failure of the world's financial system has been avoided as "deft policy saw off calamity". The solvency of the vast majority of the banks affected, or so far as is known to be affected, is being restored by recapitalisation, and the failure of another major bank such as Lehman's should be avoided. The Central Banks and Governments have recognised that the immediate requirements must take precedence over other objectives, and seem likely to develop policies appropriate to the extreme conditions. They have put in place extensive measures designed to ease liquidity, to increase credit and to reduce its costs. Other measures, such as quantitative easing, are also likely. Thus the present system will survive and credit conditions improve. In the months ahead the improved credit conditions will increase the demand for houses and prospective sellers who had not previously accepted market clearing prices will increasingly trade and transaction numbers rise. This rise in transactions will take place in a market that will still be experiencing the positive serial correlation of the recent price falls - momentum - but at some point it will switch and the momentum will reverse. When the market stops falling it will start rising! Switches in investment sentiment are fickle and impossible to determine - a knowledge or understanding of them would be a veritable philosopher's stone, - and I suspect that the switch will result from a combination of perceived over reaction, available credit, investment return and the pent-up or growing demand created by the current market seizure. An abrupt change is common in property markets. The Hillier Parker All Property Yield is rarely unchanged quarter to quarter, and peak prices or trough prices immediately reverse. In my view such a reversal in house prices will occur no earlier than Autumn 2009 and no later than Spring 2010.

**Future Progress**

We will not commission development until market conditions improve. Within the last year we have had several sites on which development could have commenced, but, because of the then prospects for the economy, we have delayed starting until market conditions improve. Thus we have no large-scale building work in progress, or committed.

Farming enjoyed an excellent 2006/07 season, particularly the arable sector, and this led to the increase in agricultural land prices. As the supply elasticity of arable products is very high, we did not expect these high prices to persist and we are disposing of the agricultural interests acquired as an adjunct to our rural development properties. We have sold one farm and part of another farm where a second part is under offer.

Planning work will continue on many of our fifteen rural development sites where we expect to gain some approvals over the coming year, although many planning regulations and their interpretation are both becoming increasingly less advantageous. Most of these sites were purchased, unconditionally i.e. without planning permission, the vast majority several years ago, when house prices were below last year's peak, and when permission is obtained, should increase in value significantly. For development or trading properties no change is made to the Company's balance sheet even when the open-market values have increased considerably. Naturally, however, the balance sheet will reflect the value of such properties on their sale or subsequent development.

Our investment portfolio has been reduced over the last few years as the Company's interests were increasingly directed to enhancing value by gaining planning change. Historically we have adopted a conservative policy and have secured long-term borrowings against a low LTV and at low margin. The investment portfolio's value will reflect the market conditions at the time which without doubt will continue to worsen, but should improve earlier than some commentators expect. When appropriate we will seek to realise investment properties as we have just done in Aberdeen at a premium to its purchase price and to its recent valuation.

The current year's results will continue to reflect the decline in the investment and residential market. The cut in interest rates is greatly beneficial and I expect that the Libor premium will continue to decline as the bailout of the banking system becomes effective. The Group has long-standing relationships with its bankers. Our main facility is a five year loan maturing in February 2011. Other facilities are with banks from whom we have had borrowings over the same properties since 1990 and 1994 respectively of which one has just renewed and the other, a two-year facility, falls due for renewal in August 2009. I expect these relationships to continue.

The mid-market share price on 24 December 2008 was 72.5p a discount of 53.7% to the NAV of 156.6p. The Board does not recommend a final dividend but will restore dividends when profitability and consideration for other opportunities and obligations permits.

**Conclusion**

Last year I concluded "The UK economy is expected to experience a major deflationary shock resulting form an unprecedented contraction of credit" which is now occurring. Recently there have been four changes for the better: the inflation occurring in oil, foods and commodity prices has been viciously reversed; Sterling has fallen significantly; interest rates are at record lows and still falling; and the authorities, who previously prevaricated, are now taking appropriate action. These factors will moderate the severity of the recession.

The recession will embrace all the "developed" economies and have a severe impact on the emerging economies, will dispose of the theory of "decoupling" and will have far-reaching political implications: the Anglo Saxon liberal market model will give ground to the European centralist model; oil exporters, particularly Russia, will have their political power attenuated and for eastern exporters, especially China, will face political upsets. Fortunately, unlike the Great Depression, protectionism will be limited and deflationary policies avoided.

Further falls in investment and residential property prices are likely, but lower interest rates and increased credit combined with changing expectations of future price changes will bring an "upturn" within nine to eighteen months.

Fortunately the recession will pass, but it will not leave its passage unmarked.

I D Lowe

CHAIRMAN 29 December 2008

The directors present their report and the group financial statements for the year ended 30 June 2008.

## Activities

The principal activities of the group are the holding of property for both investment and development purposes.

## Results and dividends

The group loss for the year after taxation amounted to £7,159,000 (2007 *profit of £524,000).* The directors do not propose a dividend in respect of the current financial year. In the prior year the company paid dividends of £326,780.

## Business review

The group is required to comply with the Enhanced Business Review disclosures required by the Companies Act 1985 as amended to comply with the EU Modernisation Directive. A full review of the group's business results for the year and future prospects is included in the Chairman's Statement within the Review of Activities on pages 2 to 5 and Future Progress on pages 13 to 14. In accordance with legislation the accounts have been prepared in accordance with IFRS as adopted by the EU ("adopted IFRS") for the first time. An explanation of how the transition to adopted IFRS has affected the financial position, financial performance and cashflows of the group is given in note 24.

### Key performance indicators

The key performance indicators for the group are property valuations, planning progress and the stability of house prices, all of which are discussed in the Chairman's Statement.

### Principal risks and uncertainties

There are a number of potential risks and uncertainties, which have been identified within the business which could have a material impact on the group's long-term performance.

***Planning and development***

The increasing development profile of the group places increased emphasis on the planning stage of each project. The group seeks to minimise this risk with its firmly established risk control strategy, which includes detailed research and planning advice. On obtaining planning consent a decision will be taken on progressing the project on its own or with a joint development partner. At all stages the company seeks professional advice, conducts thorough diligence and continually monitors each development.

***Property values***

Conditions in the UK property market represent uncertainties in the operating environment rather than risks which can be managed. Nevertheless, many of the investment properties held by the group have development prospects or a development angle which will insulate them against the full effect of any general investment downgrade of commercial property.

**Principal risks and uncertainties (continued)**

***Tenant relationships***

All property companies have exposure to the covenant of their tenants as rentals drive capital values as well as providing the necessary cash flow to service debt. The group seeks to minimise exposure to any single sector or tenant across the portfolio and continually monitors payment performance.

***Availability of funding***

The group is dependent upon bank borrowings for current and future property transactions. Bank facilities are negotiated and tailored to each project in terms of quantum and timing. Any intended borrowings for future projects will be at or below traditional levels of gearing and therefore will be readily available.

***Management of funding risk***

The group seeks to ensure that adequate resources are available to meet the short and long term funding requirements of the group at all times and that any funding risks arising from group activities be effectively identified and managed.

***Management of interest rate risks***

Group borrowings are primarily in relation to and secured by properties, which are held as investments or are being developed. As and when future development projects are undertaken banking facilities will be negotiated and tailored to each project. Interest rate risk is constantly monitored and reviewed. This risk is managed by securing floating rate debt, which can be fixed from time to time by the group or by the use of interest rate swaps or other financial instruments.

***Environmental policy***

The group recognises the importance of its environmental responsibilities, monitors its impact on the environment and designs and implements policies to reduce any damage that might be caused by the group's activities.

## Directors

The directors who held office at the year end and their interests in the company's share capital are set out below:

**Beneficial interests - Ordinary shares of 20p each**

| | **Percentage held** | **30 June 2008** | 30 June 2007 |
|---|---|---|---|
| | | **£** | £ |
| ID Lowe | 78.5 | 9,324,582 | 9,324,582 |
| MJ Baynham | 6.1 | 730,191 | 730,191 |
| RJ Pearson | - | - | - |
| AJ Hartley | - | - | - |

**Beneficial interests - Floating rate loan stock 2010**

| | | | |
|---|---|---|---|
| ID Lowe | 100.0 | 1,350,000 | 1,000,000 |

No rights to subscribe for shares or debentures of group companies were granted to any of the directors or their immediate families or exercised by them during the financial year.

On 26 August 2008, AJ Hartley was appointed as a director.

## Suppliers

It is the company's policy to settle suppliers' invoices within sixty days of their receipt.

## Donations

The group made charitable donations of £65,080 (2007: £33,040)

## Disclosure of information to auditors

The directors who held office at the date of approval of the Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the company auditors are unaware; and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the company auditors are aware of that information.

## Auditors

In accordance with Section 489 of the Companies Act 2006, a resolution for the re-appointment of KPMG Audit Plc as auditors of the company is to be proposed at the forthcoming Annual General Meeting.

By Order of the Board

**MJ Baynham**
Secretary

29 December 2008

## Statement of directors' responsibilities for the preparation of financial statements

The directors are responsible for preparing the Annual Report and the group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. As required by the AIM rules of the London Stock Exchange, they are required to prepare the group financial statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the parent company financial statements in accordance with UK accounting standards and applicable laws (United Kingdom Generally Accepted Accounting Practice).

The group financial statements are required by law and IFRSs as adopted by the EU to present fairly the financial position and the performance of the group; the Companies Act 1985 provides in relation to such financial statements that references in the relevant part of that Act to financial statements giving a true and fair view are references to their achieving a fair presentation.

The parent company financial statements are required by law to give a true and fair view of the state of affairs of the parent company.

In preparing each of the group and parent company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- for the group financial statements, state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- for the parent company financial statements, state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the parent company financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group and the parent company will continue in business.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the parent company and enable them to ensure that its financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

KPMG Audit Plc
Saltire Court
20 Castle Terrace
Edinburgh EH1 2EG
United Kingdom

**Independent auditors' report to the members of Caledonian Trust PLC**

We have audited the group and parent company financial statements ("the financial statements") of Caledonian Trust PLC for the year ended 30 June 2008 which comprise the group income statement, the group and parent company balance sheets, the group cash flow statement, the group statement of recognised income and expense and the related notes. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

**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 (IFRSs) as adopted by the EU and for preparing the parent company financial statements in accordance with applicable law and UK accounting standards (UK Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities on page 18.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements 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 financial statements. The information given in the Directors' Report includes that specific information presented in the Chairman's Statement that is cross referred from the Business Review 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 the other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

## Independent auditors' report to the members of Caledonian Trust PLC (continued)

### 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 financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the group financial statements, and of whether the accounting policies are appropriate to the group's and 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 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 IFRSs as adopted by the EU, of the state of the group's affairs as at 30 June 2008 and of its loss for the year then ended;
- the parent company financial statements give a true and fair view in accordance with UK Generally Accepted Accounting Practice of the state of the parent company's affairs as at 30 June 2008;
- the financial statements have been prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

**KPMG Audit Plc**
Chartered Accountants
Registered Auditor

29 December 2008

## Caledonian Trust PLC

**Group income statement for the year ended 30 June 2008**

| | Note | 2008<br>£000 | 2007<br>£000 |
|---|---|---|---|
| Gross rental income | | **793** | 658 |
| Service charge income | | **20** | 26 |
| Dilapidation income | | **29** | - |
| Property charges - occupied properties | | **(158)** | (144) |
| Property charges - unoccupied properties | | **(76)** | (196) |
| **Net rental and related income** | | **608** | 344 |
| Proceeds from sale of trading properties | | **175** | 1,477 |
| Carrying value of trading properties sold | | **(70)** | (1,074) |
| **Profit from disposal of trading properties** | | **105** | 403 |
| Administrative expenses | | **(840)** | (809) |
| Other income | | **61** | 163 |
| Other expenses | | **(14)** | (51) |
| **Net other income** | | **47** | 112 |
| **Net operating (loss)/profit before investment property disposals and valuation movements** | 5 | **(80)** | 50 |
| Profit on disposal of investment properties | | **-** | 16 |
| Valuation gains on investment properties | | **709** | 867 |
| Valuation losses on investment properties | | **(7,870)** | (225) |
| **Net valuation (losses)/gains on investment properties** | | **(7,161)** | 642 |
| **Operating (loss)/profit** | | **(7,241)** | 708 |
| Financial income | 7 | **30** | 257 |
| Financial expenses | 7 | **(664)** | (567) |
| **Net financing costs** | | **(634)** | (310) |
| **(Loss)/profit before taxation** | | **(7,875)** | 398 |
| Income tax credit | 8 | **716** | 126 |
| **(Loss)/profit for the financial period attributable to equity holders of the company** | | **(7,159)** | 524 |

| | | | |
|---|---|---|---|
| **(Loss)/earnings per share** | | | |
| Basic (loss)/earnings per share (pence) | 9 | **(60.25p)** | 4.41p |
| Diluted (loss)/earnings per share (pence) | 9 | **(60.25p)** | 4.41p |

## Caledonian Trust PLC

**Consolidated statement of recognised income and expense for the year ended 30 June 2008**

| | **2008** **£000** | 2007 £000 |
|---|---|---|
| Change in the fair value of equity securities available for sale | **(30)** | (2) |
| **Net loss recognised directly in equity** | **(30)** | (2) |
| (Loss)/profit for the period | **(7,159)** | 524 |
| **Total recognised income and expense for the period attributable to equity holders of the parent** | **(7,189)** | 522 |

## Caledonian Trust PLC

### Consolidated balance sheet as at 30 June 2008

| | Note | **2008** **£000** | 2007 £000 |
|---|---|---|---|
| **Non current assets** | | | |
| Investment property | 10 | 16,915 | 24,076 |
| Property, plant and equipment | 11 | 22 | 17 |
| Investments | 12 | 11 | 41 |
| **Total non-current assets** | | 16,948 | 24,134 |
| **Current assets** | | | |
| Trading properties | 13 | 11,383 | 10,767 |
| Trade and other receivables | 14 | 434 | 539 |
| Cash and cash equivalents | 15 | 42 | 824 |
| **Total current assets** | | 11,859 | 12,130 |
| **Total assets** | | 28,807 | 36,264 |
| **Current liabilities** | | | |
| Trade and other payables | 16 | (462) | (655) |
| Interest bearing loans and borrowings | 17 | (987) | (696) |
| Income tax liabilities | 20 | - | - |
| | | (1,449) | (1,351) |
| **Non current liabilities** | | | |
| Interest bearing loans and borrowings | 17 | (8,750) | (8,400) |
| Deferred tax liabilities | 20 | - | (716) |
| | | (8,750) | (9,116) |
| **Total liabilities** | | (10,199) | (10,467) |
| **Net assets** | | 18,608 | 25,797 |
| **Equity** | | | |
| Issued share capital | 21 | 2,377 | 2,377 |
| Capital redemption reserve | 22 | 175 | 175 |
| Share premium account | 22 | 2,745 | 2,745 |
| Retained earnings | 22 | 13,311 | 20,500 |
| **Total equity attributable to equity holders of the parent** | | 18,608 | 25,797 |

The financial statements were approved by the board of directors on 29 December 2008 and signed on its behalf by:

**ID Lowe**
Director

**Consolidated cash flow statement for the year ended 30 June 2008**

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| **Cash flows from operating activities** | | |
| **(Loss)/profit for the period** | (7,159) | 524 |
| Adjustments for : | | |
| (Profit) on sale of investment property | - | (16) |
| Losses/(gains) on fair value adjustment of investment property | 7,161 | (642) |
| Loss on sale of plant and equipment | - | 4 |
| Depreciation | 7 | 7 |
| Net finance expense | 642 | 310 |
| Income tax credit | (716) | (126) |
| **Operating cash flows before movements in working capital** | (65) | 61 |
| (Increase) in trading properties | (616) | (3,733) |
| Decrease in trade and other receivables | 105 | 429 |
| (Decrease)/increase in trade and other payables | (192) | 164 |
| **Cash generated from operating activities** | (768) | (3,079) |
| Interest paid | (665) | (558) |
| Interest received | 22 | 257 |
| **Cash flows from operating activities** | (1,411) | (3,380) |
| **Investing activities** | | |
| Proceeds from sale of investment property | - | 613 |
| Acquisition of property, plant and equipment | (12) | (6) |
| **Cash flows from investing activities** | (12) | 607 |
| **Financing activities** | | |
| Proceeds from new long term borrowings | 641 | 1,720 |
| Dividends paid | - | (327) |
| **Cash flows from financing activities** | 641 | 1,393 |

## Caledonian Trust PLC

| | | |
|---|---|---|
| **Net decrease in cash and cash equivalents** | (782) | (1,380) |
| Cash and cash equivalents at beginning of year | 824 | 2,204 |
| **Cash and cash equivalents at end of year** | 42 | 824 |

**Notes to the consolidated financial statements**

**1 Reporting entity**

Caledonian Trust PLC is a company domiciled in the United Kingdom. The consolidated financial statements of the company for the year ended 30 June 2008 comprise the company and its subsidiaries (together referred to as "the Group"). The Group's principal activities are the holding of property for both investment and development purposes.

**2 Statement of Compliance**

The financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the EU ("Adopted IFRSs") that are effective at 30 June 2008.

The financial statements were approved by the directors and authorised for issue on 29 December 2008.

**3 Basis of preparation**

The Company is preparing its financial statements in accordance with Adopted IFRSs for the first time and consequently has applied IFRS 1 – First time adoption of International Financial Reporting Standards. An explanation of how the transition to Adopted IFRSs has affected the reported financial position, financial performance and cash flows of the Group is provided in note 25. This note includes reconciliations of equity and profit or loss for comparative periods reported under UK GAAP to those reported for those periods under Adopted IFRSs. The company has elected not to restate business combinations prior to the date of transition to Adopted IFRSs.

The financial statements are prepared on the historical cost basis except for available for sale financial assets and investment properties which are measured at their fair value.

The preparation of the financial statements in conformity with Adopted IFRSs requires the directors to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

These financial statements have been presented in pounds sterling which is the company's functional currency. All financial information has been rounded to the nearest pounds thousand.

*Going concern*

The group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Chairman's Statement on pages 2 to 5 and pages 13 to 14.

Note 18 to the financial statements includes the group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit risk and liquidity risk.

The Directors have prepared cash flow forecasts for the group and company for a period of 12 months from the date of authorisation of these financial statements. The group's forecasts and projections reflect the Directors' plans for the coming year and include rental income and expected income from the sales of properties and development land. These forecasts show that the group should be able to operate within the level of its current loan facilities. When performing sensitivity analysis on these projections the group has also considered the cash flow position assuming that sales of property are confined to those which are currently

## 3 Basis of preparation (continued)

unconditional. On the assumption that completion monies from these sales are received when due then this also shows that the group should be able to operate within its facilities. Certain of the group's loan facilities are demand facilities or are due for renewal within the next 12 months and the directors will enter into renewal negotiations with the banks in due course. The group is regularly in discussion about its future borrowing needs and no matters have been drawn to its attention to suggest that renewal may not be forthcoming on acceptable terms.

The group's main banking facility is subject to financial covenants and other conditions which the group monitors regularly. These covenants and conditions are sensitive to changes in rental income, interest rates and the value of properties. Whilst the directors cannot envisage all possible circumstances, the directors believe that, taking account of reasonably foreseeable adverse movements in rental income, interest or property values, the group has sufficient resources available to it, including additional support from the major shareholder if necessary, to ensure continued compliance with these conditions.

In preparing their sensitivity analyses the directors have taken account of the unusual circumstances prevailing in the property market at the current time and recognise that the current economic climate creates uncertainty over the timing and amount of ultimate realisation of these cashflows, in particular in respect of the sale of certain assets. However, after making enquiries, the Directors have a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

**Areas of estimation uncertainty and critical judgements**

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements is contained in the following notes:

- Valuation of investment properties (note 10)

  The valuation of properties is subjective and based on similar transactions in the market, rental yields and development potential. The company's directors are experienced in dealing with such properties. Valuations at the balance sheet date are based on independent external valuations.

- Valuation of trading properties (note 13)

  Trading properties are carried at lower of cost and net realisable value. The net realisable value of such properties is based on the amount the company is likely to achieve in a sale to a third party which is dependent on availability of planning consent and demand for sites which is influenced by the housing and property markets.

- Taxation (note 8)

As noted in note 8, the company have treated a dilapidations payment from a tenant as a capital receipt and accordingly no taxation has been provided in these financial statements. In the event that HMRC do not agree with this treatment the directors will vigorously challenge any such contrary view. The tax that would be payable if the receipt were to be treated as revenue is approximately £615,000.

## 4 Accounting policies

The accounting policies below have been applied consistently to all periods presented and in preparing the opening balance sheet as at 1 July 2006 for the purposes of transition to Adopted IFRSs.

**Basis of consolidation**

The financial statements incorporate the financial statements of the company and all its subsidiaries. Subsidiaries are entities controlled by the group. Control exists when the group has the power to determine the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date it ceases.

**Revenue**

Rental income from properties leased out under operating leases is recognised in the income statement on a straight line basis over the term of the lease. Costs of obtaining a lease and lease incentives granted are recognised as an integral part of total rental income and spread over the period from commencement of the lease to the earliest termination date on a straight line basis.

Revenue from the sale of trading properties is recognised in the income statement on the date at which the significant risks and rewards of ownership are transferred to the buyer with proceeds and costs shown on a gross basis.

**Other income**

Other income comprises income from agricultural land and other miscellaneous income

**Finance income and expenses**

Finance income and expenses comprise interest payable on bank loans and other borrowings. All borrowing costs are recognised in the income statement using the effective interest rate method. Interest income represents income on bank deposits using the effective interest rate method.

**Taxation**

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case the charge / credit is recognised in equity. Current tax is the expected tax payable on taxable income for the current year, using tax rates enacted or substantively enacted at the reporting date, adjusted for prior years under and over provisions.

Deferred tax is provided using the balance sheet liability method in respect of all temporary differences between the values at which assets and liabilities are recorded in the financial statements and their cost base for taxation purposes. (Deferred tax includes current tax losses which can be offset against future capital gains.) As the carrying value of the group's investment properties is expected to be recovered through eventual sale rather than rentals, the tax base is calculated as the cost of the asset plus indexation. Indexation is taken into account to reduce any liability but does not create a deferred tax asset.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

**Investment properties**

Investment properties are properties owned by the group which are held either for long term rental growth or for capital appreciation or both. Properties transferred from trading properties to investment properties are revalued to fair value at the date on which the properties are transferred.

When the Group begins to redevelop an existing investment property for continued future use as investment property, the property remains an investment property, which is measured based on fair value model, and is not reclassified as property, plant and equipment during the redevelopment.



## 4 Accounting policies (continued)

**Investment properties (continued)**

The cost of investment property includes the initial purchase price plus associated professional fees. Borrowing costs directly attributable to the acquisition or construction of qualifying assets are capitalised during the period of construction. Subsequent expenditure on investment properties is only capitalised to the extent that future economic benefits will be realised.

Investment property is measured at fair value at each balance sheet date. External independent professional valuations are prepared at least once every three years. The fair values are based on market values, being the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arms length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

Any gain or loss arising from a change in fair value is recognised in the income statement.

**Purchases and sales of investment properties**

Purchases and sales of investment properties are recognised in the financial statements at completion which is the date at which the significant risks and rewards of ownership are transferred to the buyer.

**Property, plant and equipment**

Property, plant and equipment are stated at cost, less accumulated depreciation and any provision for impairment. Depreciation is provided on all property, plant and equipment at varying rates calculated to write off cost to the expected current residual value by equal annual instalments over their estimated useful economic lives. The principal rates employed are:

| | | |
|---|---|---|
| Office equipment | - | 11 – 33.3 per cent |
| Fixtures and fittings | - | 10 per cent |
| Motor vehicles | - | 33.3 per cent |

**Trading properties**

Trading properties held for short term sale or with a view to subsequent disposal in the near future are stated at the lower of cost or net realisable value. Cost is calculated by reference to invoice price plus directly attributable professional fees. Net realisable value is based on estimated selling price less estimated cost of disposal.

**Financial assets**

***Trade and other receivables***

Trade and other receivables are initially recognised at fair value and then stated at amortised cost.

**Financial instruments**

***Available for sale financial assets***

The group's investments in equity securities are classified as available for sale financial assets. They are initially recognised at fair value plus any directly attributable transaction costs. Subsequent to initial recognition they are measured at fair value and changes therein, other than impairment losses, are recognised directly in equity. The fair value of available for sale investments is their quoted bid price at the balance sheet date. When an investment is disposed of, the cumulative gain or loss in equity is recognised in profit or loss. Dividend income is recognised when the company has the right to receive dividends either when the share becomes ex dividend or the dividend has received shareholder approval.



---

## 4 Accounting policies (continued)

**Financial instruments (continued)**

***Cash and cash equivalents***

Cash includes cash in hand, deposits held at call (or with a maturity of less than 3 months) with banks, and bank overdrafts. Bank overdrafts that are repayable on demand and which form an integral part of the Group's cash management are shown within current liabilities on the balance sheet and included with cash and cash equivalents for the purpose of the statement of cash flows.

**Financial liabilities**

***Trade payables***

Trade payables are non-interest-bearing and are initially measured at fair value and thereafter at amortised cost.

***Interest bearing loans and borrowings***

Interest-bearing loans and bank overdrafts are initially carried at fair value less allowable transactions costs and then at amortised cost.

**Segmental analysis**

The company's principal activity consists of holding property for investment and development. The directors believe that these activities comprise one business unit and consequently segmental analysis is not considered necessary.

**IFRS not yet effective**

The following IFRS have been adopted and so will require to be applied in future periods and are expected to affect the entity

*Amendment to IAS 1 presentation of financial statements: A revised presentation*. The standard will require the group to present a statement of comprehensive income and may require additional disclosures.

*Amendment to IAS 27 Consolidated and Separate financial statements and IFRS 3 (revised) Business combinations*. These amendments require changes to the accounting for business combinations and will only affect the entity if it makes acquisitions in the future.

## 5 Operating (loss)/profit

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| The operating (loss)/profit is stated after charging/(crediting): | | |
| Depreciation | **7** | 7 |

| | | |
|---|---|---|
| Fees paid to auditors | | |
| - audit of the financial statements | **11** | 11 |
| - audit of financial statements of subsidiaries pursuant to legislation | **18** | 16 |
| | ====== | ====== |



## 6 Employees and employee benefits

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| Employee remuneration | | |
| Wages and salaries | **321** | 345 |
| Social security costs | **37** | 37 |
| Other pension costs | **52** | 52 |
| | **410** | 434 |
| | ====== | ====== |

Other pension costs represent contributions to defined contribution plans

The average number of employees during the year was as follows:

| | **No.** | No. |
|---|---|---|
| Management | **2** | 2 |
| Administration | **2** | 2 |
| Other | **2** | 9 |
| | **6** | 13 |
| | ====== | ====== |

The directors consider that key management personnel are the company's directors. Compensation is shown below:

| | **2008** | 2007 |
|---|---|---|
| *Remuneration of directors* | **£000** | £000 |
| Directors' emoluments | **244** | 247 |
| Company contributions to money purchase pension schemes | **48** | 48 |
| | ====== | ====== |

The aggregate of emoluments of the highest paid director was £113,600 *(2007 - £112,787)* and company pension contributions of £27,500 *(2007 - £27,500)* were made to a money purchase scheme on his behalf.

Retirement benefits are accruing to 2 *(2007 - 2)* directors under money purchase schemes.

## 7 Finance income and finance costs

| | 2008 £000 | 2007 £000 |
|---|---|---|
| **Finance income** | | |
| Interest receivable: | | |
| - on bank balances | **30** | 257 |
| | ===== | ====== |
| **Finance costs** | | |
| Interest payable: | | |
| - Bank loans and overdrafts | **577** | 484 |
| - Loan stock repayable within five years | **87** | 83 |
| | **664** | 567 |
| | ===== | ====== |



## 8 Income tax

| | 2008 £000 | 2007 £000 |
|---|---|---|
| *Recognised in the income statement* | | |
| UK corporation tax – current period | **-** | - |
| | **-** | - |
| Deferred tax – effect of change in rate | **(52)** | - |
| Deferred tax – current period | **(664)** | (126) |
| Total income tax credit in income statement | **(716)** | (126) |
| | ====== | ====== |

| | 2008 £000 | 2007 £000 |
|---|---|---|
| (Loss)/profit for the year | **(7,159)** | 524 |
| Income tax credit | **(716)** | (126) |
| (Loss)/profit before tax | **(7,875)** | 398 |
| | ====== | ====== |

Reconciliation of effective tax rate

| | 2008 % | 2008 £000 | 2007 % | 2007 £000 |
|---|---|---|---|---|
| (Loss)/profit before tax | | **(7,875)** | | 398 |
| | | ====== | | ====== |

| | | | | |
|---|---|---|---|---|
| Current tax | **29.5** | **(2,323)** | 30.0 | 119 |
| *Effects of:* | | | | |
| Expenses not deductible for tax purposes | **(0.1)** | **15** | 1.5 | 6 |
| Capital gains tax indexation (restricted) | **(10.3)** | **816** | (36.7) | (146) |
| Deferred tax change in rate | **(0.7)** | **52** | | - |
| Deferred tax asset not recognised | **(9.2)** | **724** | | - |
| Other differences | **-** | **-** | (26.4) | (105) |
| Total tax credit | **(9.0)** | **(716)** | (31.6) | (126) |

In the case of deferred tax in relation to investment property revaluation surpluses, the base cost used is historical book cost and includes allowances or deductions which may be available to reduce the actual tax liability which would crystallise in the event of a disposal of the asset.



## 8 Income tax (continued)

### Factors affecting the future tax charge

The group received a dilapidations payment from the former tenants of an investment property amounting to £2,100,000 during the year ended 30 June 2005. The payment was made to fulfil the tenant's obligations under the repairing lease held by them. The directors are presently progressing a development brief for the island site of which the property forms part which once formally adopted by the Planning Authority will enhance the value. Accordingly the repair work to the property has not been carried out and it is unlikely that they will be undertaken. The receipt was treated as a capital receipt for taxation purposes on which basis no taxation was payable or has been provided. HMRC has queried the tax treatment of this receipt and there is an ongoing dialogue with HMRC local inspector on the matter. The directors continue to be of the opinion that the receipt is a capital receipt and accordingly no taxation has been provided in these financial statements. In the event that HMRC do not agree with this treatment the directors will vigorously challenge any such contrary view. The tax that would be payable if the receipt were to be treated as revenue is approximately £615,000.

## 9 Loss/(earnings) per share

Basic (loss)/earnings per share is calculated by dividing the (loss)/earnings attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period as follows:

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| (Loss)/profit for financial period | (7,159) | 524 |
| | ======== | ====== |
| | No. | No. |
| Weighted average no of shares: | | |
| For basic earnings per share and for diluted earnings per share | 11,882,923 | 11,882,923 |
| | ======== | ======== |
| Basic (loss)/earnings per share | (60.25p) | 4.41p |
| Diluted (loss)/earnings per share | (60.25p) | 4.41p |

The diluted loss per share is the same as the basic loss per share as there are no diluted shares.

## 10 Investment properties

| | 2008 | 2007 |
|---|---|---|
| | **£000** | £000 |
| **Valuation** | | |
| At 30 June 2007 | **24,076** | 24,031 |
| Revaluation in year | **(7,161)** | 642 |
| Sold in year | **-** | (597) |
| **Valuation at 30 June 2008** | **16,915** | 24,076 |

The carrying amount of investment property is the fair value at the balance sheet date as determined by external independent valuations at open market value made by Montagu Evans, Rettie and Co, and Allsop, independent property consultants, at 30 June 2008. The properties have been valued individually in accordance with the definition of market value and good practice guidelines set out in the 6th Edition of the Royal Institution of Chartered Surveyors valuation and appraisal manual. In this regard, market value is defined as "the estimated amount for which a property should exchange between a willing buyer and willing seller in an arm's length transaction after proper marketing wherein the parties had acted knowledgeably, prudently and without compulsion". The valuers have taken into account rental values and development potential.

Fair values were calculated having regard to recent transactions for similar properties.

Investment properties comprise a number of commercial properties, some of which are leased to third parties with an initial rental period. Subsequent renewals are negotiated with the tenant.

The cumulative amount of interest capitalised in respect of the group's investment properties is £869,467 *(2007: £869,467)*.

Certain of the company's investment properties with a carrying value of £13,615,000 *(2007: £20,420,000)* are secured against bank borrowings and as such on disposal of investment properties a proportion of proceeds are remitted to reduce bank borrowings

## Notes to the consolidated financial statements (continued)

### 11 Property, plant and equipment

| | Motor vehicles £ | Fixtures and fittings £ | Other equipment £ | Total £ |
|---|---|---|---|---|
| **Cost** | | | | |
| At 30 June 2006 | 13 | 196 | 20 | 229 |
| Additions in year | 2 | - | 4 | 6 |
| Disposals in year | - | (151) | - | (151) |
| **At 30 June 2007** | **15** | **45** | **24** | **84** |
| At 30 June 2007 | 15 | 45 | 24 | 84 |
| Additions in year | - | 3 | 9 | 12 |
| **At 30 June 2008** | **15** | **48** | **33** | **96** |
| **Depreciation** | | | | |
| At 30 June 2006 | 13 | 191 | 4 | 208 |
| Charge for year | 1 | 1 | 5 | 7 |
| Disposals in year | - | (148) | - | (148) |
| **At 30 June 2007** | **14** | **44** | **9** | **67** |
| At 30 June 2007 | 14 | 44 | 9 | 67 |
| Charge for year | 1 | 1 | 5 | 7 |
| **At 30 June 2008** | **15** | **45** | **14** | **74** |
| **Net book value** | | | | |
| At 30 June 2006 | - | 5 | 16 | 21 |
| At 30 June 2007 | 1 | 1 | 15 | 17 |
| **At 30 June 2008** | **-** | **3** | **19** | **22** |

**Notes to the consolidated financial statements (continued)**

## 12 Investments

| | 2008 £000 | 2007 £000 |
|---|---|---|
| *Available for sale investments* | | |
| At the start of the year | **41** | 43 |
| Loss on available for sale investments recognised in equity | **(30)** | (2) |
| Available for sale financial assets | **11** | 41 |

## 13 Trading properties

| | 2008 £000 | 2007 £000 |
|---|---|---|
| At start of year | **10,767** | 7,034 |
| Additions | **686** | 4,807 |
| Disposals | **(70)** | (1,074) |
| At end of year | **11,383** | 10,767 |

Trading properties with carrying value of £2,474,000 (2007: £2,408,000) are secured against the Group's bank borrowings.

## 14 Trade and other receivables

| | 2008 £000 | 2007 £000 |
|---|---|---|
| *Amounts falling due within one year* | | |
| Other debtors | **282** | 396 |
| Prepayments and accrued income | **152** | 143 |
| | **434** | 539 |

The company's exposure to credit risks and impairment losses relating to trade receivables is given in note 18.

## 15 Cash and cash equivalents

| | 2008 £000 | 2007 £000 |
|---|---|---|

| | | |
|---|---|---|
| Cash | **42** | 824 |
| | **======** | ====== |

Cash and cash equivalents comprise cash at bank and in hand. Cash deposits are held with UK banks. The carrying amount of cash equivalents approximates to their fair values. The company's exposure to credit risk on cash and cash equivalents is regularly monitored.

## 16 Trade and other payables

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| Accruals and other creditors | **462** | 655 |
| | ====== | ====== |

The Group's exposure to currency and liquidity risk relating to trade payables is disclosed in note 18.

## 17 Other interest bearing loans and borrowings

The Group's interest bearing loans and borrowings are measured at amortised costs. More information about the Group's exposure to interest rate risk and liquidity risk is given in note 18.

*Current liabilities*

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| Current portion of secured bank loans | **987** | 696 |
| | ======= | ======= |

*Non current liabilities*

| | **2008** | 2007 |
|---|---|---|
| Non-current portion of secured bank loans | **7,400** | 7,400 |
| Floating rate unsecured loan stock | **1,350** | 1,000 |
| | **8,750** | 8,400 |
| | ======= | ======= |

*Terms and debt repayment schedule*

Terms and conditions of outstanding loans and loan stock were as follows:

| | | | **2008** | | 2007 | |
|---|---|---|---|---|---|---|
| | Currency | Nominal interest rate | **Fair value £000** | **Carrying amount £000** | Fair value £000 | Carrying amount £000 |
| Secured bank loans | GBP | LIBOR + 0.95 to 3.00%<br>Base +1.5% | **7,400** | **7,400** | 7,400 | 7,400 |
| Floating rate unsecured loan stock | GBP | Base + 3% | **1,350** | **1,350** | 1,000 | 1,000 |
| | | | **8,750** | **8,750** | 8,400 | 8,400 |

The bank loans are secured by standard securities and charges over the assets of certain subsidiaries and by an unlimited guarantee by Caledonian Trust PLC.



## 18 Financial instruments

### Fair values

*Fair values versus carrying amounts*

The fair values of financial assets and liabilities, together with the carrying amounts shown in the balance sheet, are as follows:

| | **30 June 2008** | | 30 June 2007 | |
|---|---|---|---|---|
| | **Fair value** | **Carrying amount** | Fair value | Carrying amount |
| | **£000** | **£000** | £000 | £000 |
| Available for sale financial assets | **11** | **11** | 41 | 41 |
| Loans and receivables | **346** | **346** | 539 | 539 |
| Cash and cash equivalents | **42** | **42** | 824 | 824 |
| Secured bank loans | **8,387** | **8,387** | 8,096 | 8,096 |
| Loan from related party | **1,350** | **1,350** | 1,000 | 1,000 |
| Trade and other payables | **462** | **462** | 654 | 654 |
| | **10,598** | **10,598** | 11,154 | 11,154 |

***Estimation of fair values***

The following methods and assumptions were used to estimate the fair values shown above:

***Available for sale financial assets –*** as such assets are listed, the fair value is determined at the market price.

***Trade and other receivables/payables*** – the fair value of receivables and payables with a remaining life of less than one year is deemed to be the same as the book value.

***Cash and cash equivalents*** – the fair value is deemed to be the same as the carrying amount due to the short maturity of these instruments.

***Secured bank loans and other loans*** – the fair value is based on the book value as the interest rate charged reflects the fair value of the borrowings.

### Overview of risks from its use of financial instruments

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk

The Board of Directors has overall responsibility for the establishment and oversight of the company's risk management framework and oversees compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group.



## 18 Financial instruments (continued)

The Board's policy is to maintain a strong capital base so as to cover all liabilities and to maintain the business and to sustain its development.

The Board of Directors also monitors the level of dividends to ordinary shareholders.

There were no changes in the Group's approach to capital management during the year.

Neither the company nor any of its subsidiaries are subject to externally imposed capital requirements.

The group's principal financial instruments comprise bank loans, cash and short term deposits. The main purpose of these financial instruments is to finance the group's operations.

As the group operates wholly within the United Kingdom, there is currently no exposure to currency risk.

The main risks arising from the group's financial instruments are interest rate risks and liquidity risks. The board reviews and agrees policies for managing each of these risks, which are summarised below

### Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Group's receivables from customers, cash held at banks and its available for sale financial assets.

*Trade receivables*

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each tenant. The majority of rental payments are received quarterly in advance which reduces the group's exposure to credit risk on trade receivables.

*Other receivables*

Other receivables consist of amounts due from a company in which the group holds a minority investment and an amount due from a previous tenant in respect of dilapidations.

The Group reviews the carrying value of trade and other receivables and will establish an impairment provision only if there are indications that the debt is not recoverable.

*Available for sale financial assets*

The Group does not actively trade in available for sale financial assets. The Group's investments had a fair value of £11,420 at 30 June 2008 *(2007: £41,000)* and so the Group does not have significant exposure to credit risk in relation to these assets.

*Bank facilities*

At the year end the company had loan facilities of £8.4 million *(2007: £8.1 million)* available.

*Exposure to credit risk*

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

## 18 Financial instruments (continued)

### Credit risk (continued)

| | Carrying value | |
|---|---|---|
| | **2008** | 2007 |
| | **£000** | £000 |
| Available for sale investments | **11** | 41 |
| Other receivables | **282** | 396 |
| Cash and cash equivalents | **42** | 824 |
| | **335** | 1,261 |

A table showing the ageing of receivables at the balance sheet date is not disclosed as the company does not have trade receivables as there are no arrears in respect of rental income at the year end or previous year end. This position is representative of the position throughout the year and the company's other receivables are in respect of dilapidations and were not due at the balance sheet date.

The company does not have an allowance for impairment on trade receivables as, based on historical experience, management does not consider that such an impairment is required.

Credit risk for trade receivables at the reporting date was all in relation to property tenants in United Kingdom.

The company's exposure is spread across a number of customers.

### Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due without incurring unacceptable losses or risking damage to the Company's reputation.

The group's main banking facility is subject to financial covenants and other conditions which the group monitors regularly. These covenants and conditions are sensitive to changes in rental income, interest rates and the value of properties. Whilst the directors cannot envisage all possible circumstances, the directors believe that, taking account of reasonably foreseeable adverse movements in rental income, interest or property values, the group has sufficient resources available to it, including additional support from the major shareholder if necessary, to ensure continued compliance with these conditions.

## 18 Financial instruments (continued)

### Liquidity risk (continued)

The group's exposure to liquidity risk is given below

| 30 June 2008 | Carrying amount | Contractual cash flows | 6 months or less | 6-12 months | 1-2 years | 2-5 years | More than 5 years |
|---|---|---|---|---|---|---|---|
| Secured bank loans | 8,387 | 9,236 | 1,183 | 196 | 392 | 7,465 | - |
| Floating rate unsecured loan stock | 1,350 | 1,512 | 40 | 41 | 1,431 | - | - |
| Trade and other payables | 282 | 282 | 282 | - | | - | - |

| 30 June 2007 | Carrying amount | Contractual cash flows | 6 months or less | 6-12 months | 1-2 years | 2-5 years | More than 5 years |
|---|---|---|---|---|---|---|---|
| Secured bank loans | 8,096 | 9,900 | 985 | 289 | 578 | 8,048 | - |
| Floating rate unsecured loan stock | 1,000 | 1,171 | 43 | 43 | 1,085 | - | - |
| Trade and other payables | 396 | 396 | 396 | - | - | - | - |

### Market risk

Market risk is the risk that changes in market prices, such as interest rates, will affect the company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

*Interest rate risk*

The Group borrowings are at floating rates of interest based on LIBOR or Base Rate.

The interest rate profile of the Group's borrowings as at the year end was as follows:

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| Floating rate instruments – financial liabilities | **9,737** | 9,096 |
| | ======= | ======= |

The weighted average interest rate of the floating rate borrowings was 7.20% *(2007: 7.29%)*.

A 1% movement in interest rates would be expected to change the Group's annual net interest charge by £97,372 *(2007: £90,964)*.

## 19 Operating leases

*Leases as lessors*

The group leases out its investment properties under operating leases. The future minimum receipts under non cancellable operating leases are as follows:

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| Less than one year | **625** | 618 |
| Between one and five years | **2,139** | 2,270 |
| Greater than five years | **5,246** | 5,742 |
| | **8,010** | 8,650 |

The amounts recognised in income and costs for operating leases are shown on the face of the income statement.

## 20 Income tax and deferred tax

At 30 June 2008, the company has a potential deferred tax asset of £265,000 of which relates to differences between the carrying value of investment properties and the tax base. In addition the group has tax losses which would result in a deferred tax asset of £458,000. This has not been recognised due to the uncertainty over future taxable profits. In 2007 the deferred tax liability is as a result of revaluations. In 2008, the asset has arisen as a result of the accounting base being below the tax base as a result of property revaluations.

**Movement in temporary differences in the year**

| £'000 | Balance 1 Jun 06 at 30% | Recognised in profit or loss | Balance 30 Jun 07 at 30% | Recognised in profit or loss lo | **Balance 30 Jun 08 at 28%** |
|---|---|---|---|---|---|
| | £000 | £000 | £000 | £000 | £000 |
| Investment properties | 950 | (77) | 873 | (873) | **-** |
| Tax losses | (108) | (49) | (157) | 157 | **-** |
| Total | 842 | 126 | 716 | (716) | **-** |

**Movement in unrecognised deferred tax asset**

| £'000 | Balance 1 Jun 06 at 30% | Additions | Balance 30 Jun 07 | Additions | **Balance 30 Jun 08 at 28%** |
|---|---|---|---|---|---|
| | £000 | £000 | £000 | £000 | **£000** |
| Investment properties | - | - | - | 265 | **265** |
| Tax losses | - | - | - | 458 | **458** |

| | | | | | |
|---|---|---|---|---|---|
| Total | | - | - | 723 | **723** |

**Notes to the consolidated financial statements (continued)**

| 21 | **Issued share capital** | **30 June 2008** | | **30 June 2007** | |
|---|---|---|---|---|---|
| | | **No** | **£000** | No. | £000 |
| | **Authorised** | | | | |
| | Ordinary shares of 20p each | **20,000,000** | **4,000** | 20,000,000 | 4,000 |
| | **Issued and fully paid** | | | | |
| | Ordinary shares of 20p each | **11,882,923** | **2,377** | 11,882,923 | 2,377 |

Holders of ordinary shares are entitled to dividends declared from time to time, to one vote per ordinary share and a share of any distribution of the company's assets.

| 22 | **Capital and reserves** | **Share capital** | **Capital redemption reserve** | **Share premium account** | **Retained earnings** | **Total** |
|---|---|---|---|---|---|---|
| | | **£000** | **£000** | **£000** | **£000** | **£000** |
| | At 1 July 2006 | 2,377 | 175 | 2,745 | 20,303 | **25,600** |
| | Total recognised income and expense | - | - | - | 524 | **524** |
| | Dividends | - | - | - | (327) | **(327)** |
| | At 30 June 2007 | 2,377 | 175 | 2,745 | 20,500 | **25,797** |
| | At 1 July 2007 | 2,377 | 175 | 2,745 | 20,500 | **25,797** |
| | Total recognised income and expense | - | - | - | (7,189) | **(7,189)** |
| | Dividends | - | - | - | - | **-** |
| | At 30 June 2008 | 2,377 | 175 | 2,745 | 13,311 | **18,608** |

Following transition to IFRS , the balance on the revaluation reserve was transferred to the retained earnings reserve as any changes in the value of properties are reflected in the income statement.

In the year ended 30 June 2007, the following dividends were paid:

| | | £000 |
|---|---|---|
| Final dividend in respect of year to 30 June 2006 | 1.75p/share | 208 |
| Interim dividend in respect of year to 30 June 2007 | 1.00p/share | 119 |
| | | 327 |



## 23 Related parties

*Transactions with key management personnel*

Transactions with key management personnel consist of compensation for services provided to the company. Details of this are given in note 6.

*Other related party transactions*

The group and company has unsecured floating rate loan stock due to Leafrealm Limited, a company of which ID Lowe is the controlling shareholder. This is on normal commercial terms. Leafrealm received £88,000 *(2007 - £83,000)* interest in respect of its holding of Floating Rate Unsecured Loan Stock. The balance due to this party at the year end was £1,350,000 (2007: £1,000,000).

## 24 Explanation of Transition to adopted IFRS

### Balance sheet

| | Note | 1 July 2006 Previous GAAP £000 | 1 July 2006 Effect of transition to IFRS £000 | 1 July 2006 IFRS £000 | 30 June 2007 Previous GAAP £000 | 30 June 2007 Effect of transition to IFRS £000 | 30 June 2007 IFRS £000 |
|---|---|---|---|---|---|---|---|
| **Non current assets** | | | | | | | |
| Investment property | | 24,031 | - | 24,031 | 24,076 | - | 24,076 |
| Property, plant and equipment | | 21 | - | 21 | 17 | | 17 |
| Investments | (a) | 43 | - | 43 | 43 | (2) | 41 |
| **Total non-current assets** | | 24,095 | - | 24,095 | 24,136 | (2) | 24,134 |
| **Current assets** | | | | | | | |
| Trading properties | | 7,034 | - | 7,034 | 10,767 | - | 10,767 |
| Trade and other receivables | | 968 | - | 968 | 539 | - | 539 |
| Cash and cash equivalents | | 2,204 | - | 2,204 | 824 | - | 824 |
| **Total current assets** | | 10,206 | - | 10,206 | 12,130 | - | 12,130 |
| **Total assets** | | 34,301 | - | 34,301 | 36,266 | (2) | 36,264 |
| **Current liabilities** | | | | | | | |
| Trade and other payables | | (483) | - | (483) | (655) | - | (655) |
| Interest bearing loans and borrowings | | (1,696) | - | (1,696) | (696) | - | (696) |
| Income tax liabilities | | - | - | - | - | - | - |
| | | (2,179) | - | (2,179) | (1,351) | - | (1,351) |
| **Non current liabilities** | | | | | | | |
| Interest bearing loans and borrowings | | (5,680) | - | (5,680) | (8,400) | - | (8,400) |
| Deferred tax liabilities | | - | (842) | (842) | - | (716) | (716) |
| | | (5,680) | (842) | (6,522) | (8,400) | (716) | (9,116) |
| **Total liabilities** | | (7,857) | (842) | (8,701) | (9,751) | (716) | (10,467) |
| **Net assets** | | 26,442 | (842) | 25,600 | 26,515 | (718) | 25,797 |
| **Equity** | | | | | | | |
| Issued share capital | | 2,377 | - | 2,377 | 2,377 | - | 2,377 |
| Other reserves | | 2,920 | - | 2,920 | 2,920 | - | 2,920 |
| Retained earnings | | 21,145 | (842) | 20,303 | 21,218 | (718) | 20,500 |
| **Total equity attributable to equity holders of the parent** | | 26,442 | (844) | 25,600 | 26,515 | (718) | 25,797 |

## 24 Explanation of Transition to adopted IFRS (continued)

**Income statement**

| | Previous GAAP 30 June 2007 | Effect of transition to IFRS | IFRS |
|---|---|---|---|
| | £000 | £000 | £000 |
| Revenue from properties | 684 | - | 684 |
| Property charges - occupied properties | (144) | - | (144) |
| Property charges - unoccupied properties | (196) | - | (196) |
| **Net rental and related income** | 344 | - | 344 |
| Proceeds from sale of trading properties | 1,477 | - | 1,477 |
| Carrying value of trading properties sold | (1,074) | - | (1,074) |
| **Profit from disposal of trading properties** | 403 | - | 403 |
| Other income | 163 | - | 163 |
| Other expenses | (51) | - | (51) |
| **Net other income** | 112 | - | 112 |
| Administrative expenses | (809) | - | (809) |
| **Operating profit before investment property disposals and valuation movements** | 50 | - | 50 |
| Profit on disposal of investment properties | 16 | - | 16 |
| Valuation gains on investment properties | - | 867 | 867 |
| Valuation losses on investment properties | - | (225) | (225) |
| **Operating profit** | 66 | 642 | 708 |
| Financial income | 257 | - | 257 |
| Financial expenses | (567) | - | (567) |
| **(Loss)/profit before taxation** | (244) | 642 | 398 |
| Income tax expense | - | 126 | 126 |
| **(Loss)/profit for the financial period attributable to equity holders of the company** | (244) | 768 | 524 |
| **(Loss)/earnings per share** | | | |
| Basic (loss)/earnings per share (pence) | (2.05p) | | 4.41p |
| Diluted (loss)/earnings per share (pence) | (2.05p) | | 4.41p |

---

**Explanation of Transition to adopted IFRS (continued)**

(a) The treatment of investment property revaluations – under UK GAAP gains or losses on revaluation of investment properties were recorded in a revaluation reserve. Under IFRS revaluation gains and losses are recorded in the income statement. The impact of this on the opening balance sheet was that the revaluation reserve was reduced by £6,625,414 and retained earnings increased by a similar amount. For the year ended 30 June 2007, property revaluations which would have been credited or debited directly to reserves have been credited directly to the income statement.

(b) Accounting for investments – under UK GAAP investments were held at cost less permanent impairments in value. Under IFRS investments are held as available for sale financial assets and are held at fair value with gains or losses recorded directly in equity unless there is a permanent impairment which is recorded in the income statement. This resulted in a £1,593 reduction in equity at 30 June 2007.

(c) Deferred taxation – under UK GAAP deferred taxation on investment property revaluation gains was not provided for in the balance sheet unless there was a commitment to sell the property. Under IFRS deferred tax provisions are made for the tax that would potentially be payable on the sale of investment properties where their carrying value is different from their cost for tax purposes. Where current tax losses can be offset against future capital gains, the related deferred tax asset has been recognised and offset against the deferred tax liability. This has resulted in additional provision of £841,853 in the opening balance sheet and £716,520 in the balance sheet as at 30 June 2007.

Other than presentational differences, there are no material differences between the cash flow statement presented under UK GAAP and the statement of cashflows under IFRS.

## Caledonian Trust PLC

### Company balance sheet at 30 June 2008

| | Note | £000 | 2008 £000 | £000 | 2007 £000 |
|---|---|---|---|---|---|
| **Fixed assets** | | | | | |
| **Tangible assets** | | | | | |
| Investment properties | 3 | | **5,690** | | 5,761 |
| Equipment and vehicles | 4 | | **22** | | 17 |
| | | | **5,712** | | 5,778 |
| Investments | 5 | | **11,168** | | 11,200 |
| | | | **16,880** | | 16,978 |
| **Current assets** | | | | | |
| Stock of development property | 6 | **3,272** | | 2,839 | |
| Debtors | 7 | **18,042** | | 23,689 | |
| Cash at bank and in hand | | **29** | | 793 | |
| | | **21,343** | | 27,321 | |
| **Creditors** | | | | | |
| Amounts falling due within one year | 8 | **(11,907)** | | (11,427) | |
| **Net current assets** | | | **9,436** | | 15,894 |
| **Total assets less current liabilities** | | | **26,316** | | 32,872 |
| **Creditors** | | | | | |
| Amounts falling due after more than one year | 8 | | **(7,750)** | | (7,400) |
| **Net assets** | | | **18,566** | | 25,472 |
| **Capital and reserves** | | | | | |
| Called up shares capital | 9 | | **2,377** | | 2,377 |
| Share premium account | | | **2,745** | | 2,745 |
| Capital redemption reserve | | | **175** | | 175 |
| Revaluation reserves: | | | | | |
| Property | 10 | | **2,266** | | 2,337 |
| Investments | 10 | | **1,305** | | 1,305 |
| Profit and loss account | 10 | | **9,698** | | 16,533 |
| **Shareholders' funds** | | | **18,566** | | 25,472 |

The financial statements were approved by the board of directors on 29 December 2008 and signed on its behalf by:

**Caledonian Trust PLC**

**ID Lowe**
Director

## 1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements.

### Basis of preparation

The financial statements are prepared under the historical cost convention as modified by the revaluation of investment properties and investments and in accordance with applicable accounting standards. The company has not presented its own profit and loss account in accordance with section 230 of the Companies Act 1985.

The company has taken advantage of the exemption contained within FRS 8 and has not disclosed details of transactions or balances with companies the results of which are included within the consolidated accounts of Caledonian Trust PLC.

### Properties

Properties held by the group are classified within fixed assets as investment properties, or current assets if held as trading stock.

### Investment properties

In accordance with Statement of Standard Accounting Practice No 19, investment properties are revalued annually at open market value either by the directors or by independent professional advisers. Independent professional valuations are prepared at least once every three years. All surpluses and deficits on valuation are taken directly to revaluation reserve except that any permanent diminution in the value of the investment property is taken to the profit and loss account for the year. No depreciation or amortisation is provided in respect of freehold investment properties.

This treatment may be a departure from the Companies Act requirements concerning the depreciation of fixed assets. However, the properties are not held for consumption but for investment and the directors consider that systematic annual depreciation would be inappropriate. The accounting policy adopted is therefore necessary for the accounts to give a true and fair view. Depreciation or amortisation is only one of the many factors reflected in the annual valuation and the amount which might otherwise have been shown cannot be separately identified or quantified.

## 1 Accounting policies (continued)

### Properties held as stock

Properties held as trading stock are stated at the lower of cost or net realisable value.

For properties previously held as investment properties which are now held for development and reclassified as current assets, cost is considered to be the latest valuation prior to their reclassification. This is not in accordance with Schedule 4 to the Companies Act 1985, which requires current assets to be included at the lower of cost and net realisable value, and which would therefore require such properties to be restated on the basis of historical cost when they are reclassified. The directors consider that compliance with this requirement would fail to give a true and fair view of the profit and loss to the company on disposal of such properties from current assets, since such profit or loss would be dependent on the classification of the asset immediately prior to sale. The effect of this departure is to increase both the value of properties held for resale and the balance on the revaluation reserve by £36,249 at 30 June 2008 *(2007 - £36,249)*.

### Investments

Investments in subsidiary undertakings are included in the balance sheet of the company at valuation representing the net asset value of the undertaking concerned. Surpluses or deficits arising on revaluations are taken to the revaluation reserve except in the case of impairments which are taken to the profit and loss account. The revaluation reserve is not distributable.

Other investments are held at cost unless they are considered to have suffered a permanent impairment. Such impairments are taken to the profit and loss account.

### Dividends on shares presented within shareholders' funds

Dividends unpaid at the balance sheet date are only recognised as a liability at that date to the extent that they are appropriately authorised and are no longer at the discretion of the company. Unpaid dividends that do not meet these criteria are disclosed in the notes to the financial statements.

### Depreciation

Tangible fixed assets, other than investment properties, are depreciated by equal instalments over their estimated useful lives at the following rates:

| | | |
|---|---|---|
| Fixtures and fittings | - | 10% |
| Office equipment | - | 11% - 33% |
| Motor vehicles | | $33^1/_3$% |

## 1 Accounting policies (continued)

### Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19.

### Post retirement benefits

The group makes payments to defined contribution pension schemes on behalf of certain employees. The amount charged to the profit and loss account represents the contributions payable to the schemes in respect of the accounting period.

## 2 Profit of parent company

As permitted by Section 230 of the Companies Act 1985, the profit and loss account of the parent company is not presented as part of these financial statements. The parent company's loss for the financial period after taxation was £803,966.

## 3 Investment properties

| | **£000** |
|---|---|
| *Valuation* | |
| At 30 June 2007 | 5,761 |
| Revaluation in year | (71) |
| **Valuation at 30 June 2008** | 5,690 |

The carrying amount of investment property is the fair value at the balance sheet date as determined by external independent valuations at open market value made by Montagu Evans, independent property consultants, and Rettie & Co, independent property consultants, at 30 June 2008.

Fair values were calculated having regard to recent transactions for similar properties.

Investment properties comprise a number of commercial properties, some of which are leased to third parties with an initial rental period. Subsequent renewals are negotiated with the tenant.

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| The historical cost of investment properties included at valuation is: | **3,424** | 3,424 |

======== =======

The cumulative amount of interest capitalised for the company is £343,000 *(2007 - £343,000).*

## 4 Tangible fixed assets

| | Motor vehicles £000 | Office equipment £000 | Other equipment £000 | Total £000 |
|---|---|---|---|---|
| **Cost** | | | | |
| At 30 June 2007 | 15 | 45 | 24 | 84 |
| Additions in year | - | 3 | 9 | 12 |
| **At 30 June 2008** | **15** | **48** | **33** | **96** |
| **Depreciation** | | | | |
| At 30 June 2007 | 13 | 45 | 9 | 67 |
| Charged in year | 1 | 1 | 5 | 7 |
| **At 30 June 2008** | **14** | **46** | **14** | **74** |
| **Net book value** | | | | |
| **At 30 June 2008** | **1** | **2** | **19** | **22** |
| At 30 June 2007 | 2 | 0 | 15 | 17 |

## 5 Investments

| | Shares in subsidiary investments £000 | Listed investments £000 | Total £000 |
|---|---|---|---|
| **Cost** | | | |
| At 30 June 2007 and 2008 | 4,933 | 43 | 4,976 |
| Impairment | - | (32) | (32) |
| | 4,933 | 11 | 4,944 |
| **Revaluation surplus** | | | |
| At 30 June 2007 and 2008 | 6,224 | - | 6,224 |
| **Net book value** | | | |
| **At 30 June 2008** | **11,157** | **11** | **11,168** |
| At 30 June 2007 | 11,157 | 43 | 11,200 |

| Subsidiary undertaking | % held | Activity |
|---|---|---|
| Caledonian Scottish Developments Ltd | 100% | Property Development |
| South Castle Properties Ltd | 100% | Property Investment |
| Caledonian Stoneywood Ltd | 100% | Investment Holding Company |
| Caledonian City Developments Ltd | 100% | Property Development |
| West Castle Properties Ltd | 100% | Property Investment |
| Melville Management Ltd | 100% | Property Investment |

All the principal subsidiary undertakings are registered in Scotland except Caledonian City Developments Limited and Caledonian Stoneywood Ltd, which are registered in England and Wales. A list of the other subsidiary undertakings will be included in the company's next annual return.

The company holds an unlisted investment of 19.9% of the share capital of Bedrocks Limited, a leisure activity operator registered in Scotland.

The market value of the company's listed investments at 30 June 2008 was £11,000 (2007 £43,000)

## 6 Stock of development property

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| Properties held for resale or development | **3,272** | 2,839 |

## 7 Debtors

| | **2008** | 2007 |
|---|---|---|
| | **£000** | £000 |
| *Amounts falling due within one year* | | |
| Prepayments and accrued income | **40** | 21 |
| | **40** | 21 |
| *Amounts falling due in more than one year* | | |
| Amounts owed by subsidiary undertakings | **18,002** | 23,668 |
| | **18,042** | 23,689 |

## 8 Creditors

| | | |
|---|---|---|
| *Amounts falling due within one year* | | |
| Bank loans | **290** | - |
| Amounts owed to subsidiary undertakings | **11,294** | 10,919 |
| Other creditors and accruals | **323** | 508 |
| | **11,907** | 11,427 |
| *Amounts falling due after more than one year* | | |
| Bank loans | **6,400** | 6,400 |
| Floating rate unsecured loan stock | **1,350** | 1,000 |
| | **7,750** | 7,400 |

**Analysis of debt**

| | | |
|---|---|---|
| Debt can be analysed as falling due: | | |
| In one year or less, or on demand | **290** | - |
| Between one and two years | **-** | 1,000 |
| Between two and five years | **7,750** | 6,400 |
| | **8,040** | 7,400 |

The company's bank loans are secured by standard securities and floating charges over the assets of the company and certain subsidiaries and by an unlimited guarantee from Caledonian

Trust PLC. Interest charged on these loans is based on margins ranging from 0.95% over the prevailing London Interbank Offer Rate to 1.5% over the Bank of Scotland base rate.

The floating rate unsecured loan stock was renegotiated during the year and is now repayable in July 2010. Interest is charged at a margin of 3% over the Bank of Scotland base rate.

## 9 Share capital

| | 2008 No. | 2008 £000 | 2007 No. | 2007 £000 |
|---|---|---|---|---|
| **Authorised** | | | | |
| Ordinary shares of 20p each | **20,000,000** | **4,000** | 20,000,000 | 4,000 |
| **Allotted, called up and fully paid** | | | | |
| Ordinary shares of 20p each | **11,882,923** | **2,377** | 11,882,923 | 2,377 |

## 10 Reserves

| | Revaluation reserves Property £000 | Revaluation reserves Investments £000 | Profit and loss account £000 |
|---|---|---|---|
| Balance at 30 June 2007 | 2,337 | 1,305 | 16,533 |
| Property revaluation in year | (71) | - | - |
| Loss for the financial year | - | - | (6,835) |
| **Balance at 30 June 2008** | **2,266** | **1,305** | **9,698** |

The movement in the valuation of investment properties has been reflected through the revaluation reserve as the directors are of the opinion that such decreases are temporary.

## 11 Reconciliation of movements in shareholders' funds

| | 2008 £000 | 2007 £000 |
|---|---|---|
| Retained loss for the financial year | **(6,835)** | (692) |
| Dividends paid | **-** | (327) |
| Revaluation (deficit)/surplus | **(71)** | 47 |
| Net decrease in shareholders' funds | **(6,906)** | (972) |
| Opening shareholders' funds | **25,472** | 26,444 |
| **Closing shareholders' funds** | **18,566** | 25,472 |

## 12 Related party transactions

The group and company have unsecured floating rate loan stock due to Leafrealm Limited, a company of which ID Lowe is the controlling shareholder. This is on normal commercial terms. Leafrealm which received £88,000 *(2007 - £83,000)* interest in respect of its holding of Floating Rate Unsecured Loan Stock. The balance due to this party at the year end was £1,350,000 (2007: £1,000,000).