the **Local Shopping** reit plc

Section 1: Overview

Section 2: How We Performed

Section 3: Management and Governance

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The Local Shopping REIT plc

The Local Shopping REIT plc ("LSR") is a major owner of local retail property in the UK, listed on the London Stock Exchange.

Our investment objective is to provide our shareholders with an attractive and growing level of income, with additional capital growth through active asset management.

We are the first specialist start-up Real Estate Investment Trust ("REIT") to launch in the UK and intend to become the leading owner of local retail property in the UK.

Our investment policy is to acquire local shops in urban and suburban areas, investing in neighbourhood and convenience properties throughout the UK. Our portfolio typically comprises shops that are well established in their local communities, although we will invest in new developments of local shops where these are supported by existing or newly built residential property.

We believe in sustaining the local trading community nationwide and dealing with all our stakeholders in a fair and open manner.

LSR at a Glance

Operating Highlights*

- Portfolio has increased in size to 632 properties, with 1,976 letting units
- 151 acquisitions showing a total increase of 4% over purchase price
- 33 new lettings secured generating an annual rental income of £353,000 (3.5% above market rent)
- 87 rent reviews, lease renewals and surrender and re-lettings carried out increasing rent by £159,306 per annum, an average uplift of 14.3% (10.0% above market rent)
- Corporate acquisition of Gilfin Property Holdings Ltd for £12.85m, using the Company's tax exempt REIT status and generating £2m negative goodwill

* From 28 March 2007 (date of last published valuation).

Financial Highlights

- Successful admission to trading on the main market of the London Stock Exchange, raising £160m in May 2007
- Net Asset Value (NAV) 156p per share
- Loss before tax of £4.3m
- Market value of portfolio grown to £249.3m, valuation of properties held at 28 March 2007 fell by 4.1%
- Rent roll up to £17.1m
- Average initial yield on purchase since IPO of 7.34% – above IPO target of 7%
- Total debt of £98.1m, reflecting an LTV of 40%. £130m of undrawn facilities remain with an average maturity in excess of eight years
- Dividend of 3.419p per share paid on 3 January 2008 to shareholders on the register on 14 December 2007 paid as a non-PID (normal dividend)

Portfolio Summary

Value Range	No. of Properties	Value £m	Equivalent Yield*
£0 – £100k	54	4.6	7.14%
£101 – £200k	222	34.4	7.07%
£201 – £500k	219	68.9	7.02%
£501k – £1m	98	70.4	6.99%
£1 – £3m	34	50.2	7.22%
£3m +	5	20.8	7.19%
Total	**632**	**249.3**	**7.08%**

* Excluding residential.

Portfolio Valuation

Average Shop Rent

Average Shop Rent

Median Property Value

The above results have been compared to 28 March 2007 which was the date on which the portfolio was last revalued. This valuation was included in the Prospectus issued in connection with the IPO.

Our Market

What is a REIT?

The first UK Real Estate Investment Trusts ("REITs") were established in the UK following Government legislation on 1 January 2007. LSR meets all the requirements of the current legislation and is well positioned to benefit from the corporation tax advantages provided by REIT status. Election to the REIT regime gives tax exempt status in respect of rental profits generated from the exempt property investment business and capital gains tax on the sale of investment properties, provided certain conditions are met.

HM Treasury's objectives for REITs were:

- to ensure returns from different forms of property investment were taxed in broadly the same way;
- to provide a liquid vehicle for investment in property;
- to provide smaller investors with access to returns from commercial property;
- to encourage a larger percentage of equity input into property investment;
- to encourage the release of assets from the balance sheet of property occupiers;
- to encourage greater professionalism in the rented housing sector; and
- to encourage supply of residential stock by providing an exit route for house-builders.

We aspire to become the REIT of choice in the local shopping sector.

What is the Local Shopping Market?

The local shopping sub-sector of the retail market caters almost exclusively for local communities and tends to serve a limited catchment area. Local shopping is focused on suburban parades in major urban centres and on the main shopping street in small town centres and villages. It can also include niche retail areas in city centres serving local or specialist needs. An important distinction from the traditional high street is that local retail tends to lack comparison shopping. In contrast it caters for top-up, meal solution and distress purchases. It is characterised by comparatively small unit sizes and a high proportion of independent traders.

Local shopping is set to benefit from a number of demographic trends including the ageing population and the drive towards creating a greener society. Local shops provide ageing consumers an opportunity for social interaction. Green issues are forcing everyone to think carefully about car travel and congestion and road charging schemes are likely to favour the local shopping market.

The market value of the sub-sector is estimated at around £20bn, equivalent to around 15% of the overall retail market. The local shopping market has traditionally been the preserve of smaller, often locally based investors. With little competition from institutional or larger property companies, the market is highly fragmented and underdeveloped. In buying in this market we are able to exploit pricing inefficiencies when properties are subject to limited, or in some cases no marketing. Our professional approach to asset management also provides us with opportunities to generate above average returns for our shareholders.

A key characteristic of the local shopping market is the affordability of rents. Research from Colliers CRE found rents were, on average, below 7% of turnover. This compares very favourably with typical high street ratios which lie in the range of 8-15% depending on the pitch and retailer. In our portfolio the average shop rent is only £13,011 pa (or £250 per week) which is under £12.00 psf.

LSR is the only REIT focused on investing in local shopping retail property. LSR has already established a leading position in the local shopping sector since its formation in January 2005, and believes that there is an opportunity for first mover advantage as the leading REIT in this sub-sector.

Local High Street, Amesbury, Wiltshire

Our Business Model

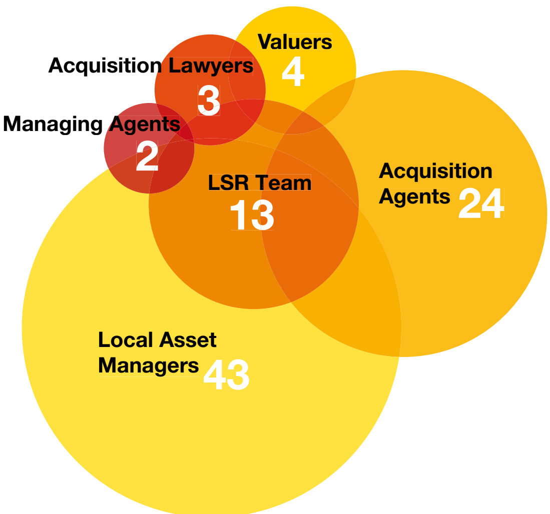
Our business model is a simple one:

- **Accretive acquisitions in sustainable locations – our average purchase yield since 28 March 2007 of 7.34%* compares with our current cost of debt of under 6.00%**
- **Using our REIT status to buy companies with deferred tax liabilities**
- **Active asset management to generate income and capital growth**
- **Robust financing: debt that is:**
  - **low cost – currently below 6.00%**
  - **long term – average unexpired term over eight years**
  - **hedged – currently 100% hedged**
- **Maintaining a prudent level of debt**
- **Recycling capital through sales of lower yielding and ex-growth assets**
- **Efficient systems for purchases, sales and asset management**

*** Excluding corporate transactions.**

We will continue to build a highly diversified portfolio, both by location and in the number of properties and tenants. Over 70% of our tenants are local independent traders. On their own an individual may represent a higher than average risk, but our spread of 1,976 tenants offers both strength and resilience.

We operate an outsourced model with a highly active national network consisting of teams of acquisition agents, acquisition lawyers, valuers, managing agents and local asset managers helping us to execute our business plan.

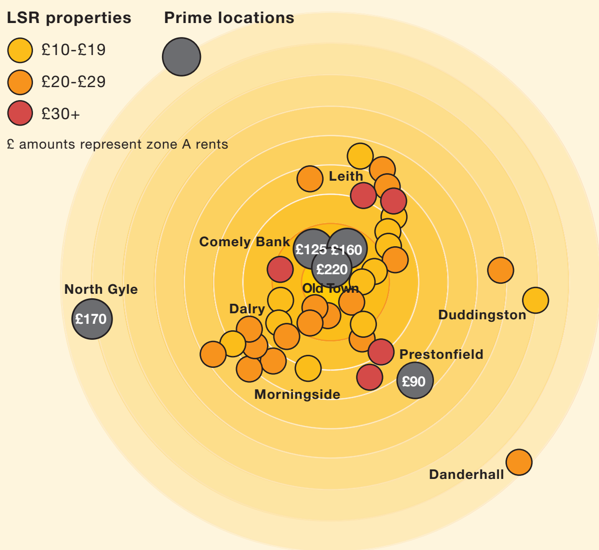


In Theory

Here we illustrate the typical locations where you might find an LSR property.

In Action – Edinburgh Case Study

Our ownerships in Edinburgh are a good example of how we buy in a major urban centre where we focus on the major arterial roads and densely populated residential neighbourhoods. The specialist high street areas of Edinburgh city centre do not fit our price/value model.



Our national network of 24 agents sourcing property acquisitions both on and off-market gives us unique access to the local shopping investment market. Their detailed local knowledge enables us to ensure the locations we buy in are sustainable and that the prevailing rental levels are affordable and allow scope for growth. Our strict investment criteria enables us to quickly identify buying opportunities.

Acquisition Criteria

- Sustainable locations
- Attractive yield
- Sourced off-market
- Low and affordable rents (<£30 psf ZA)

→ Accretive to FFO or EPS

- Asset management opportunities
- Take advantage of distressed situations
- Vacant and part-vacant

→ Capital growth and trading opportunities

- Low yielding with no growth prospects
- Poor quality buildings
- Rent >£25k pa or in excess of £30 zone A

→ Generally don't buy

Asset management is an integral part of our business. Our team continually reviews both the existing portfolio and new purchases to identify opportunities to release value from reconfigurations, adjoining land and under-used upper parts. Once opportunities are identified our agency network and additional 43 local asset managers are tasked to create further value. These gains from asset management will complement and support income from our rental business and we expect this will become a valued feature of our business model.

Hessle Road, Kingston-Upon-Hull High Street

LSR's Top Five

Top Five Tenants by Income

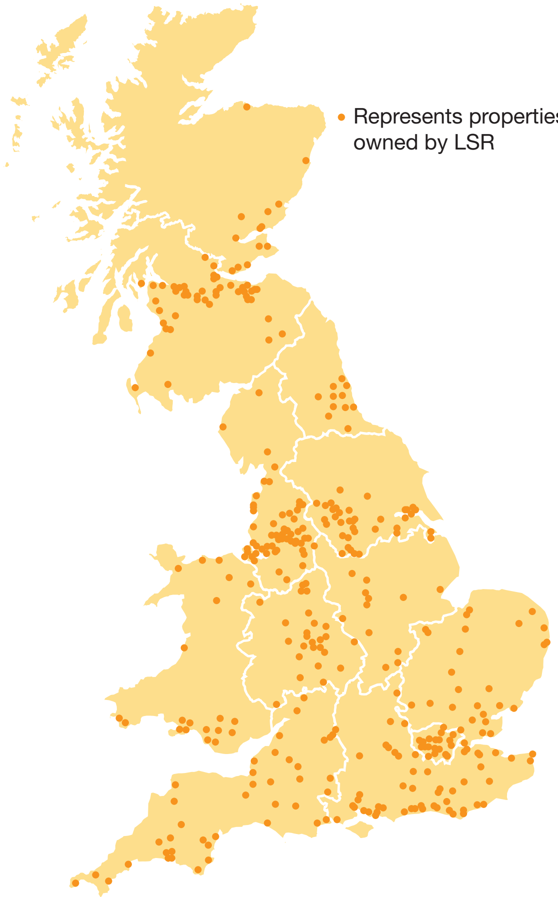
Name	No. Units	Rent	% Portfolio
Thomas Cook Ltd	13	£186,300	1.1%
Somerfield Stores Ltd	2	£128,000	0.7%
Coopland & Son (Scarborough) Ltd	8	£99,000	0.6%
Bathstore.com Ltd	2	£97,500	0.6%
First Quench Retailing Ltd	10	£97,100	0.6%

Top Five Properties by Lot Size

Name	No. Units	Value	% Portfolio
Braintree – Market St, New St and Great Square	42	£7,350,000	2.9%
Sudbury – Borehamgate Shopping Centre	39	£4,083,000	1.6%
St Helens – Four Acre Shopping Centre	14	£3,200,000	1.3%
Uckfield – 21/31 & 35/47 High Street	17	£3,150,000	1.3%
Cheveley – Cheveley Park Shopping Centre	31	£3,100,000	1.2%

Our Portfolio

Our highly diversified portfolio is located throughout the United Kingdom. Over 70% of our tenants are local independent traders. These individual traders need to make a success of their business to help support the family and their entrepreneurial spirit is the backbone of British retailing. On their own an individual may represent a higher than average risk, but our spread of 1,976 tenants offers both strength and resilience.

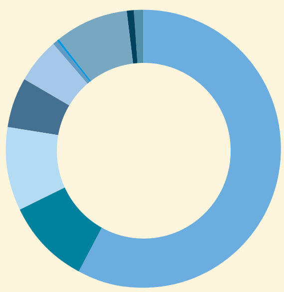


• Represents properties owned by LSR

Regional Spread*

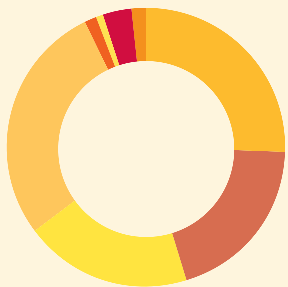
- 4.8% – East Anglia
- 4.3% – East Midlands
- 2.8% – London
- 5.6% – North
- 8.7% – North West
- 14.9% – Scotland
- 25.2% – South East
- 10.7% – South West
- 7.4% – West Midlands
- 5.4% – Wales
- 10.2% – Yorkshire and Humberside

User Types – by Planning Use*



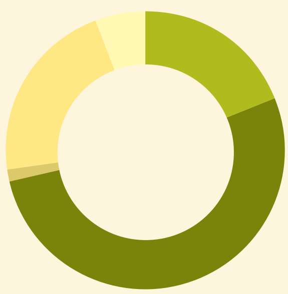
- 58.0% – A1 – Shops
- 10.0% – A2 – Financial
- 9.6% – A3 – Cafes
- 0.1% – A4 – Pubs
- 5.8% – A5 – Takeaways
- 5.2% – B1 – Offices
- 0.5% – B2 – Industrial
- 0.3% – B8 – Storage
- 8.7% – C3 – Residential
- 0.1% – D1 – Institutional
- 0.7% – D2 – Leisure
- 1.0% – Misc

Lease Expiry Profile*



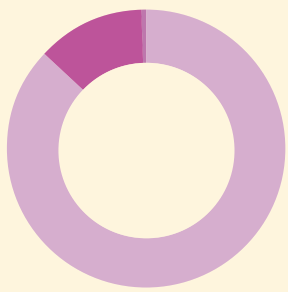
- 25.6% – 0-3yrs
- 19.8% – 3-6yrs
- 19.5% – 6-9yrs
- 28.0% – 9yrs+
- 1.5% – Vacant (residential)
- 0.7% – Vacant (deliberate)
- 3.4% – Vacant (commercial)
- 1.5% – Rent guarantee

Tenant Grade*



- 18.9% – Local company
- 52.7% – Individual
- 1.4% – Government
- 21.4% – National multiple
- 5.6% – Regional multiple

Tenure*



- 87.0% – Freehold/Virtual freehold
- 12.6% – Leasehold
- 0.4% – Short leasehold <50 years

* Shown as a % of market rent.

Chairman's Statement

I am pleased to report the full year results for the Company for the year ended 30 September 2007.

I am pleased to announce the Company's first results since listing on the London Stock Exchange covering the 12 months to 30 September 2007.

The period under review has been exciting; with the key highlight being the admission of the Company's shares to trading on the Official List of the London Stock Exchange on 2 May 2007, following a successful fundraising of £160m gross. In addition, the Company received approval from HM Revenue & Customs to become a REIT on 11 May 2007.

Since the publication of our Prospectus, the Company has been very active. We have acquired 151 properties in 106 separate transactions for a total consideration of £48.3m, increasing LSR's total portfolio to 632 properties, providing additional income and further geographical and tenant diversification. Asset management activity is also starting to produce encouraging results, with over 33 new lettings and 87 rent reviews, lease renewals and surrender and re-lettings generating over £500,000 of income. The details of these are provided in our Joint Chief Executives' business review.

Strategy

Our investment policy is to focus on investments in local shopping assets in the UK, with our core objective being to create shareholder value. Our portfolio provides good growth prospects, driven by low and affordable rental levels. We continue our aim, as set out in our Prospectus, to deliver shareholder value both from buying carefully selected assets and deploying our long-established and professional asset management skills, together with the potential for longer-term growth through the recycling of proceeds from the sale of ex-growth and lower yielding properties.

Results

Whilst meaningful year-on-year comparisons are difficult, due to the Placing and IPO in May, which changed the capital structure of the Company, the results are a good indication of the progress made.

Net rental income for the year was £11.5m, up from £5.1m in 2006. Adjusted profit before tax, which excludes the revaluation loss, and negative goodwill on acquisition was £0.116m. The corresponding basic and fully diluted loss per share was 20.0p.

Revaluation and Net Asset Value

On 30 September 2007 the portfolio was revalued at £249.3m, giving a net loss of £8.5m (4.1%) on the portfolio valuation at 28 March 2007. However, a £1.9m, or 4.0% uplift was achieved on acquisitions since that date.

The adjusted NAV of the Company is now £154.7m, which includes the fair value of our fixed rate debt.

Financing

As at 30 September 2007, Company borrowings totalled £98.1m, all of which were secured against certain of our properties. With the exception of our corporate facility, our bank borrowings expire in 2016. All the loans have interest rate hedging and the average interest rate including margin is 5.69%. The loan-to-value ratio at 30 September 2007 was 40%, with a corporate gearing ratio of 64.7%.

The fair value of debt at 30 September 2007 was £95.1m, which is £3m lower than the book value. This benefit is reflected in the Company's adjusted NAV. The Company also has undrawn banking facilities of £130m, providing ample funding for the foreseeable future.

Dividend

I am pleased to announce a final dividend of 3.419p per share, which is in line with the policy outlined at the time of the IPO. The dividend was paid on 3 January 2008, to shareholders on the register on 14 December 2007. The ex-dividend date is 12 December 2007.

Share Buyback

Due to well documented changes in the commercial property market over the past few months, the Board has implemented a strategy for the repurchase of shares, with the firm belief that this will add value to our existing shareholders. By the year end we had repurchased 2.9m shares at an average price of 129.39p. Having issued 3.9m shares at 164.86p as part consideration for the Gilfin Company acquisition, the total number of the Company's shares in issue stood at 97,539,040 (excluding Treasury Shares) on 30 September 2007. Subsequent to the year end, the Company has bought back a further 4m shares at average price of 124.43p. In total, 6.9m shares have been purchased at an average price of 126.53p, representing 6.92% of the Company's total issued share capital.

The Board believes that the Company's share price does not reflect the intrinsic value and potential of its portfolio of assets and that utilising its ability to buy back shares is a good method of enhancing shareholder value in the current market.

Convenience

Time: 06:00
Location: **High Street, Liverpool**

"I go down to my local newsagent every morning to get the paper and some milk for breakfast if we need it, and the dog takes me for a walk at the same time! It's so convenient to have a shop just round the corner that's open early, and they always know exactly what I need first thing in the morning."

LSR recognises the importance of meeting local shopping needs on your doorstep. The availability of life's essentials within walking distance of home reinforces the traditional way of life in local communities and embraces future trends such as green issues, congestion charging and an ageing society.

Chairman's Statement continued

Outlook

The Company is in a very strong financial position with low gearing levels. Our portfolio remains well balanced and diversified by both tenant type and geography. In addition, the benefits of our active asset management programmes have started to flow through and will continue to do so over the next few years. This, combined with the high yield from our diversified properties, will continue to underpin our business model.

The Company's primary focus over the next 12 months will be creating value for our shareholders through active asset management, selective purchases (both corporate, using our REIT status, and on an individual property level), share buybacks, where appropriate, and the sale of our lower yielding ex-growth properties.

As detailed in the statements below, we have made good progress on our strategy since flotation, particularly in the light of more testing and unpredictable times in the commercial property market. The management team has adapted its strategy accordingly and the measures taken, combined with the resilience of our occupier market, particularly compared to more traditional high street retailers, provide us with confidence that we are ready to act on opportunities as they present themselves and that we will create shareholder value in the future.

Grahame Whateley
Chairman

11 January 2008

Business Review

Portfolio Value		Rent Roll		No. of Properties		No. of Tenants	
30 September 2007	**£249.3m**	30 September 2007	**£17.1m**	30 September 2007	**632**	30 September 2007	**1,976**
28 March 2007	£207.7m	28 March 2007	£13.8m	28 March 2007	484	28 March 2007	1,409
+20%		+24%		+31%		+40%	

In the review below we focus our attention on the period since the portfolio was last valued on 28 March 2007 which was reported in the Prospectus.

Portfolio Performance

The portfolio was revalued at the year end at £249.3m, reflecting an equivalent yield (excluding residential element) of 7.08%. It now comprises 632 properties, with 1,976 letting units, and produces annual rental income of £17.1m.

Combined Portfolio	
Value	£249.3m
Initial yield	6.53%
Reversionary yield	7.06%
Equivalent yield	7.08%
Rent pa	£17.1m
Market rent pa	£18.5m
Commercial value	£226.7m
Residential value	£22.6m

Value Range	**No. of Properties**	**Value £m**	**Equivalent Yield***
£0 – £100k	54	4.6	7.14%
£101 – £200k	222	34.4	7.07%
£201 – £500k	219	68.9	7.02%
£501k – £1m	98	70.4	6.99%
£1 – £3m	34	50.2	7.22%
£3m +	5	20.8	7.19%
Total	**632**	**249.3**	**7.08%**

*** Excluding residential.**

This table illustrates the range of property values throughout the portfolio. The average property value is £394,000 and the median is £231,000.

The residential element of our portfolio was valued at £22.6m, with the valuation based on 90% of vacant possession value. The average value of one of the residential units in our portfolio is below £65,000.

We are also encouraged to record a positive revaluation of the acquisitions made in the period from 28 March 2007 to the year end. Their current market value of £50.3m, reflects a 4.0% increase (excluding costs of acquisition) and an equivalent yield of 7.09%.

New Purchases Since 28 March 2007

	30 September 2007	**Purchase Price**	**Change**
Value	£50.3m	£48.3m	+4.00%
Initial yield	6.63%		
Reversionary yield	7.06%		
Equivalent yield	7.09%		

The seed portfolio, as described in our Prospectus, has recorded a small fall in value of 4.1%, allowing for one sale, with the equivalent yield (excluding the residential element) moving out 33bps to 7.07%.

Seed Portfolio – Adjusted for Sales

	30 September 2007	**28 February/ 28 March 2007**	**Change**
Value	£199.0m	£207.5m	-4.10%
Initial yield	6.51%	6.32%	+0.19%
Reversionary yield	7.07%	6.68%	+0.39%
Equivalent yield	7.07%	6.74%	+0.33%
Rent pa	£13.6m	£13.8m	-1.53%
Market rent pa	£14.7m	£14.6m	+1.08%
Commercial value	£181.8m	£190.4m	-4.56%
Residential value	£17.3m	£17.1m	+1.06%

Delivery

Time: 08:45
Location: **Gorgie Road, Edinburgh**

"As the office junior, it's my job to pick up coffees for the team on my way in to the office. On a Friday our local café knows what cakes to have ready for me so that I can hand them out to the team when I get in. It's right next to the bus stop, so I don't have to go out of my way to find exactly what I need."

Service and reliability are key requirements in today's workplace. We aim to meet workers' retail needs within a local shopping centre environment, as well as delivering on our business plan to provide value and good returns for our investors.

Business Review continued

Since the year end we have made the decision to join Investment Property Databank ("IPD"), which will independently monitor our portfolio performance during the next financial year and beyond. This became effective on 30 September 2007 and we will report further on this development later in the current financial year.

Acquisitions and Sales

Since 28 March 2007, we have acquired a further 151 properties for a total consideration of £48.3m. This includes the £14.6m portfolio of properties we acquired with the purchase of Gilfin Property Holdings Limited (see below). The blended yield on these purchases, excluding Gilfin, was 7.34%, which shows we are able to continue to acquire properties on an accretive basis, even in more challenging market conditions.

The acquisition of Gilfin Property Holdings Ltd ("Gilfin") on 29 August 2007 demonstrated our ability to use the Company's tax exempt REIT status to complete corporate acquisitions where there is an unrealised capital gains position. Gilfin was a privately owned property company which we purchased for £12.85m. 50% of the consideration was satisfied in cash and 50% by the issue of 3,897,246 Ordinary Shares at £1.6486 per share. While the valuation yield on the properties was lower than our average at 6.33%, we see considerable potential to grow the rents. Additionally, we are pleased to report that, after the year end, we sold five of the properties at auction for £2.685m, at an average yield of 5.4% and £158,000 (6.3%) above the apportioned purchase price.

In the period from 28 March to 30 September 2007, we sold one property for a small profit. However, over the coming year, we intend to sell further lower-yielding, ex-growth properties. We also intend to sell a number of the market-let residential units above our shops where their sale would not prevent us from generating additional value from the property. Residential sales will also bring the benefit of reduced irrecoverable costs and lower property management and letting fees.

Asset Management

We view asset management as an integral part of our business and believe that our professional and proactive approach to it will help us deliver strong returns to our shareholders. Since the portfolio was last valued in March 2007, our team has successfully implemented the following asset management initiatives:

- Rent reviews on 65 units, increasing rents by a total of £111,297 per annum (an average uplift of 13.4%, and 8.5% above market rent);
- Lease renewals on 14 units have added a further £28,709 of rental income per annum (an average uplift of 15.7% and 7.3% above market rent);
- We have surrendered and re-let eight units, adding a total of £19,300 per annum (an average uplift of 17.5% and 22.5% above market rent);
- 33 vacant units have been re-let at a rent of £353,300 per annum (3.5% above market rent); and
- In line with our strategy to deliver value from the often under-used upper parts of our shops, we have secured planning consent for ten residential units with applications submitted for a further 28 units.

Surrender and re-lettings, where we replace a tenant whose business is struggling to pay the rent with a more effective occupier are a good example of our hands-on approach to asset management. By working with the outgoing tenant we prevent the build up of arrears while typically generating a substantial increase

Commercial Agent

Andrew R McLeod FRICS

McLeod Wright of Braintree, Essex were retained by LSR when they purchased the Crossman portfolio comprising mainly shops and offices centred in the regional towns of Chelmsford, Braintree and Sudbury.

Andrew McLeod, an experienced commercial agent, reports:

"It is refreshing to have new ideas in the management of this portfolio and the decision making process with LSR is swift and proactive. With the astute asset management team and our local knowledge and input, a very satisfactory balance is achieved."

£249.3m

Property portfolio

+151

New properties since 28 March 2007

in rent, often in advance of the next opportunity that we would have to do so under the previous lease. Our team is also continually reviewing both the existing portfolio and potential new acquisitions to identify opportunities to release value from reconfigurations, adjoining land and under-used upper parts.

While our team undertakes a large volume of asset management initiatives, we are also keeping our costs down where possible by using standard form Law Society leases on short-term lettings of smaller units, while the majority of rent reviews are dealt with in-house and without recourse to third-party determinations. In working with our tenants we abide by the Code of Practice for Commercial Leases in England and Wales, believing it is important to offer our tenants flexible leasing options which are tailored to their business needs.

Financing

Our total debt at the year end was £98.1m, reflecting a loan-to-value ratio of 40%. This debt is 100% hedged at an overall blended interest rate including margin of 5.69%. The weighted average unexpired loan term is in excess of eight years. Both our Barclays and HSBC loans have no default provisions relating to loan-to-value covenants and are on an interest only basis.

In July 2007 we repaid £26.4m of the Barclays loan, reducing the outstanding balance to £69.2m. This resulted in an interest rate margin reduction from 1.125% to 0.75% and a break fee of £294,000 which we accounted for in the current financial year.

Going forward, the Company is in a strong position, with over £130m of undrawn loan facilities, good banking relationships and attractive interest margins.

Occupier Market

As at 30 September 2007, our commercial void rate was 3.4%, up from the 2.2% reported in March 2007. Of the 62 units making up the 3.4% commercial void, there are eight units with market rents greater than £20,000 per annum, which account for 34% of the void. The letting market for these larger units, which do not conform to our core unit type, is weaker than the letting market for units within the annual £5,000-£15,000 range which remains robust. We also intend to continue to keep a number of units deliberately vacant while we seek alternative uses or look to reconfigure them. The deliberate void level, currently 0.7%, may therefore rise if suitable opportunities to add value emerge. The residential void rate has remained constant over the period, at 1.5% compared with 1.4% in March 2007, but we would expect this to fall if a number of the residential units are sold. We have seen little evidence of financial distress among our tenants in the current trading climate, with bad debts running consistently at only 1.2% of rent demanded since IPO.

Our rents remain affordable, with research by Colliers CRE suggesting rents in the local shopping market are, on average, less than 7% of turnover. Our average shop rent is only £11.99 psf, or £13,011 per annum (£250 pw) which gives us scope to continue to grow rents whilst maintaining their affordability. In the long term we believe our tenants will benefit from a number of demographic trends including the ageing population and the increased volumes of traffic on our roads.

Lawyer

Geraint Pullin Thomas, Associate Solicitor, Eversheds LLP, Cardiff

"I lead a team of ten lawyers at Eversheds which does the legal work associated with the acquisition and subsequent management of LSR's properties.

We are always impressed with the speed and efficiency of LSR's business. To make sure we are doing a great job for LSR we also have to be quick and streamlined. My team has therefore developed systems and procedures to ensure that we fully service LSR's requirements.

LSR's management team are open, friendly and very commercial. This allows us to see the big picture from their perspective and leads us to be proactive and flexible. This is vital in providing LSR with the service that they deserve and their business demands. LSR is a key client for Eversheds and we are very proud of our relationship with them. We feel that we are not just a service provider to them but a partner in their business."

Community

Time: 12:00
Location: **Bank Yard, Nottingham**

"Once the children are packed off to school we get to sit down and relax for a while over lunch and catch up on all the gossip. Many of us work so it's good to be able to meet near the office or home in order to get the most from our lunch hour. The local deli has lots of fresh ideas on the menu and I can even pick up something for dinner at the same time if I know I won't have time to cook later."

The local community forms a strong part of the UK's daily life. By building relationships with local traders and businesses, LSR aims to help sustain the local community and its social interaction to ensure that the area remains active and vital in today's competitive market place.

Business Review continued

Investment Market

Since our IPO in May 2007, we have witnessed a significant reversal in sentiment within the property market. This change has inevitably had an adverse impact on investment yields. In the local shopping market, we have noticed significant falls in the value of the larger, £1m plus individual properties, shopping parades and neighbourhood centres. However at the smaller end of the market, particularly with properties worth below £150,000, where stamp duty is not payable, we are still seeing a good volume of transactions and prices appear to be holding up.

The local shopping market is substantial, estimated to be in the region of £20bn*, and imperfect with many locally based private landlords having limited access to market knowledge and professional asset management expertise. Our national network of agents, sourcing property acquisitions both on and off-market, gives us unique access to the local shopping investment market and we look upon the downturn in the investment market as a source of potential opportunities.

* Source: Colliers CRE

Business Outlook

As a young company, the past five months have been challenging as we have adapted and developed our business model to put the Company in a position where it can operate well in a changing marketplace. Despite the difficult property investment market and uncertain financial backdrop, we look forward to the opportunities this coming year will provide. Our future success will be based upon a platform of:

- Robust financing: debt that is low cost, long term and hedged;
- A prudent level of gearing;
- Active asset management to generate income and capital growth;
- Recycling capital through sales of lower yielding and ex-growth assets;
- Share buybacks, where appropriate;
- Using our REIT status to buy companies with deferred tax liabilities;
- Accretive acquisitions in sustainable locations; and
- Efficient management systems.

Nick Gregory
Joint CEO

Mike Riley
Joint CEO

11 January 2008

Valuer

Michael Hodge FRICS, Director, Aitchison Rafferty.

"As the Director responsible for valuations I have worked closely with LSR since its original conception three years ago. I co-ordinate valuations for property acquisitions and loan security purposes across southern England liaising with LSR personnel and other consultants, especially their bankers and lawyers. LSR clearly have an excellent understanding of the local retail property sector and have established excellent relationships with all their advisers thereby ensuring a smooth acquisition process."

Financial Review

Summary of the Year

This report is prepared in accordance with International Financial Reporting Standards (IFRS). It is the first time that consolidated accounts have been prepared for the Company as, prior to the IPO, it qualified as being exempt as it was a private medium-sized group.

During the year the Company successfully floated on the London Stock Exchange, raising £160m, converted to a REIT and completed its first corporate acquisition.

Key Performance Indicators

In addition to specific measures used to monitor the property portfolio, the following key performance indicators are used by the directors to review the performance of the business and to ensure compliance with banking covenants:

	30 September 2007	30 September 2006
Interest cover*	89.1%	67.7%
Loan to value ratio	39.6%	98.8%
Adjusted NAV per share**	159p***	84p

* (based on profit before interest and tax adjusted for revaluation movements and other income).

** (based on 97,539,040 shares in issue at 30 September 2007 (2006: 4,000,000 reflecting the subdivision see below)).

*** (adjusted for fair value movements in loans not recognised).

The above show that the business has changed significantly, however, the measures still incorporate the previous capital structure. Going forward these measures should provide more meaningful assessments of the business.

Trading Results

Rents have grown from both the acquisition of new properties during the year and from increases achieved on the rents charged on the existing portfolio.

Property operating expenses, which are 12.5% (2006: 7.6%), are a larger proportion of rental income in the current year than the previous year. These costs include managing agents fees for property management services together with legal and agents fees incurred in asset management activities as well as void costs incurred on empty properties. Close to the year end the contracts with the managing agents were renegotiated, resulting in the appointment of one sole agent to manage the whole portfolio. The rate agreed is lower than previously charged: therefore these costs are expected to fall as a percentage of rents in future years. Asset management fees have also increased as the emphasis has shifted from growing the portfolio to asset management activities. Certain changes in work practices, implemented close to the year end are expected to reduce these costs in the future.

Only two properties have been sold during the year, which resulted in a profit in excess of their carrying value of £83,000 (2006: loss of £47,000).

The portfolio has continued to grow through acquisitions during the year. However, there has been a reduction in its fair value, which has been included in the income statement for the year, as required by IFRS. In accordance with the Company's accounting policy, 25% of the portfolio, together with all new purchases over the last six months, have been valued by an independent professional firm and the remainder of the portfolio has been valued by the directors who have appropriate qualifications and knowledge of the market to undertake the valuation.

Administrative expenses have been well controlled and remain the same percentage of rental income at 19.6% (2006: 19.6%). These costs also include a one-off break fee of £294,000 incurred on the loan repayment made to Barclays Capital. This cost is offset by the reduction in interest rate charged on the loan after the fall in the loan to value ratio achieved by the repayment.

Financing Costs and Available Facilities

Since the IPO the Company received interest during the year on the surplus float proceeds retained to repay part of the Barclays Capital loan and from funds awaiting investment in properties. Income has been recognised on the movement in fair value of the swaps used to hedge the interest rate exposure on the HSBC loan. None of the swaps held qualified for hedge accounting so these gains have been recognised in the income statement. During the year the Barclays Capital loan was renegotiated to a fixed rate loan, therefore, the fair value of the swaps previously held to hedge the interest rate exposure on that loan were reversed. The benefit derived from the fixed rate loan is disclosed in the notes to the accounts where the fair value of the loan is shown to be £3m lower than its carrying value.

The HSBC facility was also renegotiated in the year and increased to £150m. At the year end £30m of this facility had been utilised.

The float proceeds were used to repay a proportion of the Company's debt, in particular the mezzanine facility provided by the previous parent company, Castlemore Holdings Limited, which carried an average interest rate of 11.7%. The debt facilities retained by the Company after the repayments were made are:

- a fixed rate loan of £69m with Barclays Capital which carries an interest rate of 5.595%;
- a variable rate loan facility (not fully drawn down at the year end) of £150m with HSBC. The interest rate exposure on this loan is currently over hedged and at the year end loan-to-value ratio carries a blended interest rate of 5.69%. The interest rate charged on this loan will increase during the draw down period to a maximum of 75 base points when an LTV of 75% is reached; and
- a £10m revolving corporate credit facility with RBS which carries an interest rate of 1% above LIBOR.

At the year end none of the RBS facility had been utilised.

The Barclays Capital and HSBC facilities have no default provisions relating to loan to value covenants.

Specialist

Time: 14:25
Location: **Moorland Road, Weston-Super-Mare**

"I go down to my local salon every Friday to get a wash and blow-dry. I've been going there for years – it's so reassuring that everyone knows me and because it's really near my flat I don't even have to pay the bus fare to get there. My friend Jean and I often go together and afterwards we have a nice cup of tea and cake in the café on our way home."

With over 600 properties throughout the UK, we believe our professional management of this specialist market which is dominated by private investors will bring strong shareholder returns.

Team Work

Time: 16:00
Location: **Marsh Lane Parade, Wolverhampton**

"So much to do and so little time – I always have so many errands to run during the day and collecting the dry cleaning is just one on a long list. I try to tie it in with collecting Tom from school, and it's convenient as they're on the same street. He doesn't mind – as long as he gets a chocolate bar now and then to enjoy on the way home."

Our nationwide network of over 50 agents helps us to purchase and manage our assets. We recognise that local market expertise and a hands-on approach benefit both ourselves and the tenants. Capital growth is assisted by our efficient management systems which help us to take maximum advantage of asset management opportunities.

Financial Review continued

Corporate Acquisition

On 29 August 2007, the Company completed its purchase of the entire share capital of Gilfin Property Holdings Limited, ("Gilfin") a property investment company with a portfolio of shops in Scotland and London valued at £14.6m.

The consideration, which was provided in cash and shares, has been fair valued on the date of exchange and, when compared to the fair value of assets acquired, together with the costs incurred on the acquisition, has generated negative goodwill of over £2m. This has been credited to the income statement in the year in accordance with IFRS 3.

The loan that Gilfin had with Clydesdale bank was repaid in full on the day of completion.

Taxation

On 11 May 2007, the Group elected to join the REIT regime in the UK. As a result of joining the regime, any profits and gains from investment properties arising after the date of entry should be exempt from corporation tax provided certain conditions are met. The Group had deferred tax liabilities brought forward as at 1 October 2006, in respect of the revaluation reserve on its properties. However, entry to the REIT regime effectively extinguishes this previous deferred tax liability and the liability has been reversed in these accounts.

A conversion charge equal to 2% of the market value of the properties owned on 10 May 2007 (the day prior to joining the regime) has been provided for in these financial statements. Gilfin automatically joined the REIT regime on its acquisition and the conversion charge equal to 2% of the market value of its properties on acquisition has been provided for.

The Group is now required to analyse its business, for tax purposes, between its property rental business and other activities. The vast majority of rental income qualifies under the REIT rules as being derived from the property rental business and the directors do not consider that the Group operates any other type of business. Corporation tax remains payable on any interest income earned but the Group does not expect to pay any significant amounts of corporation tax on any of its property rental business. However, due to the availability of losses no provision for corporation tax has been made in these accounts except for the conversion charge, which must be paid in full, regardless of the Group's other activities.

Dividends

A final dividend was announced by the directors of 3.419p per share (2006: £Nil) and was paid on 3 January 2008 to shareholders on the register at 14 December 2007. In accordance with IAS 10 the Company has not provided for this dividend in these financial statements as no dividend had been declared at or before the year end. As a result of the Company's capital structure prior to IPO, the obligation for the Company to distribute 90% of its property rental income as a PID does not apply for the year ended 30 September 2007.

Investment Properties Held for Sale

At the year end certain properties have been classified as held for sale as they have been sold after the year end.

Share Capital and Reserves

Prior to the flotation of the Company, the share capital was reorganised by way of a subdivision and reclassification of its Ordinary Shares. The "A", "B" and "C" £1 Ordinary Shares were sub-divided into Ordinary 20p Shares and reclassified as "Ordinary" Shares. Following this the authorised share capital of the Company was increased to £150,000,000 via the creation of 746,000,000 new Ordinary Shares. On 2 May 2007, 91,954,023 new shares were subscribed for through the IPO and the Employee Benefit Trust subscribed for 641,521 shares at their nominal value. In addition, the Company issued a further 3,897,246 shares in order to purchase Gilfin. The Company is satisfied that all insider information has been notified.

The Company purchased a total of 2,953,750 shares at an average price of 129.39p into Treasury during the year. These shares are shown as a debit to reserves and are not included in calculating earnings and net asset value per share. A further 641,521 shares were transferred to the Employee Benefit Trust.

After flotation, the Company applied to the Companies Court to have the share premium account converted to a distributable reserve. Historically the Company has generated losses due to the level of interest paid, this conversion enables the Company to pay dividends before the historical deficits on reserves are reversed from future profits.

Cash Flows

The Company's underlying rental business generated cash inflows before the acquisition of further properties and interest payments of £8.8m (2006: £4.2m) and after interest payments cash inflows of £1.4m (2006: outflow of £0.5m).

Together with the proceeds from the flotation, further debt was drawn down and the debt repayments discussed above were made, resulting in an overall inflow of cash of £108.3m (2006: £119.2m). A further £101.3m (2006: £117.9m) has been invested in property and £6.7m in the acquisition of Gilfin.

Victoria Whitehouse
Finance Director

11 January 2008

Key Risks and Uncertainties

The Board has ultimate responsibility for identifying key risks to the business and identifying their potential and likely impact. The following have been identified as key risk areas:

- The UK's overall economic environment and significant changes in national or local economic conditions;
- Interest rates, business taxes and other factors affecting occupational demand;
- The continued availability of financing at economic rates to fund the Company's acquisition programme;
- Local planning policy;
- The legal environment and changes in legislation, central and local governmental rules and policies;
- The potential for loss of REIT status;
- Individual tenant defaults;
- The continued availability of key personnel and the skills of the Company's property managers, agents and advisers;
- Risks to the Company's reputation for ethical business practice;
- Physical risks to properties and the continued availability of insurance cover with appropriate coverage at economic rates;
- Market-led fluctuations in property values, impacting on the value of the Company's investments and its ability to continue to acquire properties at advantageous prices;
- Unforeseen property costs including maintenance and repairs;
- Local market fluctuations, resulting in rent reviews not achieving anticipated values;
- Competition from other property investors and entrants to the market;
- Significant increases in property construction and maintenance costs; and
- Health, safety and environmental issues.

The executive directors consider and evaluate key risk areas on a continuous basis. Separate meetings are held each month with relevant members of the Company's operational management team to consider operational management, asset management and refurbishment projects. The Audit Committee has formal responsibility for reviewing the Company's approach to risk management and the safeguards in place. Significant items are discussed at Board meetings.

Within this framework, the following approaches to mitigate these risks and uncertainties are in place:

- The directors and their advisers constantly monitor the property and financial markets and the wider business environment;
- The Company has the ability to flex its property acquisition and disposal plans to take account of economic trends;
- The Company's funding facilities are long-term, low cost and hedged;
- The directors monitor gearing levels to ensure they are maintained at a prudent level;
- The Company's management systems and outsourced operational approach are aimed at maximising efficiency whilst keeping overheads to a minimum;
- The directors regularly review the Company's performance against the REIT regime requirements;
- The Company and its agents keep in close touch with tenants, monitoring the potential for default and taking appropriate action at an early stage;
- The Company's staff and its agents monitor the physical condition of properties to identify potential repair issues, implementing repair and preventative maintenance programmes as necessary; and
- The directors receive reports on health, safety and environmental issues at each Board meeting.

Investment Agent

Jonathan Miles, Alder King, Partner in Charge of Cardiff Office

"We have been working closely with the LSR team since its inception and undertaken a number of investment transactions throughout the South Wales region.

Being a retained agent of a PLC has given us the opportunity to speak and present to owners and occupiers who can be difficult to get in front of. The work itself is interesting and challenging due the fact that we are dealing with relatively small lot sizes but in much larger quantities. As a result there is an added emphasis in working closer with other members of LSR's professional team (i.e. solicitors and valuers) in order that the transactions run smoothly.

An understanding of the client's requirements is essential, in that you may be dealing with a £25,000 single lock up shop in a relatively small valleys town, at the same time as dealing with a terrace of neighbourhood shops in a suburb of Cardiff.

It has been exciting being part of the team which is the first property company which has created a portfolio with the intention to convert to a REIT. As an agent this has been fascinating and has given Alder King added market profile in the South Wales market."

Corporate and Social Responsibility

Overview

We recognise that the success of our business is primarily dependent on:

- the talent and commitment of our employees;
- our partnerships with national and local advisors; and
- the well-being of businesses that occupy our properties and the communities in which they operate.

These factors are fully taken into account at Board level and throughout the management of the business and are reflected in all our activities.

We recognise the importance of the effective management of health and safety and environmental considerations in relation to our workforce, partners, tenants and the local community.

Employees

With a relatively small workforce, we rely on constant and effective communication throughout the business. Regular meetings are held to review portfolio performance, investments and disposals and specific property issues and developments. The need for a two-way flow of information is firmly embedded in our culture and our employees are consulted and informed on market conditions and investment strategy.

Our employee reward policies are designed to enable us to attract and retain the skills we need to run a first-class operation and, in particular, to recognise excellent contribution and generally align rewards to the success of the business.

We have in place firm anti-discrimination policies and we are also committed to the development of our people wherever appropriate. We support our staff in the development of their knowledge and skills, including attendance of formal education and training events and programmes.

Health, Safety and Welfare

We believe that the health, safety and welfare of our employees is superior to all other considerations. We recognise the particular risks faced by our staff when visiting remote sites. In such situations, staff are required to act within written guidelines, maintaining awareness that their welfare is the overriding consideration. The Company's health and safety record is considered at all the Board's regular meetings.

In managing our properties, we take proper account of the welfare considerations of their occupants. Our property managers and contractors ensure that all maintenance and repair works conform to relevant regulations. We undertake regular checks of gas and electrical installations within the residential elements of our portfolio, in conformance with regulatory requirements, addressing reported items and maintaining an ongoing programme of improvement works.

Business Ethics

Our ability to operate successfully in our market is largely dependent on the maintenance of our reputation for integrity and our efficient approach to doing business. We therefore require our employees and those who act on our behalf to behave and transact business on behalf of LSR in accordance with the highest professional standards. This includes complying with the regulations of any professional body to which they are affiliated. These requirements apply equally to dealings with third parties, professional advisers and tenants.

The Company has in place internal procedures enforcing the model code, anti-money laundering regulations, and data protection principles, as well as customer care and external complaint guidelines. A "whistle blowing" procedure is in place, enabling employees to notify perceived irregularities to members of the Board. Whilst such matters would ordinarily be reported through the Company Secretary, employees may raise their concerns directly with an independent non-executive director.

Partnerships

Critical to our business model is the construction and maintenance of effective partnerships at local and national level. Such alliances include:

- property sales and acquisition agents covering each locality in the UK;
- regional and local property managers;
- regional teams of property valuers;
- highly responsive arrangements with selected funding banks;
- legal advisers and support teams;
- local architects, planning consultants, project managers and quantity surveyors; and
- regional property maintenance and construction teams.

These teams are complemented by the valuable input of our corporate finance and legal advisors, as well as the support provided by our marketing, public relations and IT & communications consultants.

Whilst we employ only 13 members of staff, we engaged with 300 individuals during the year besides our core team of 50 agents and advisers. Given the importance of these relationships to our business model, we undertake a systematic communications programme to ensure that our partners are kept informed about LSR's achievement, plans and strategic development. Communication is both formal and informal, ranging from our monthly newsletter to regular meetings to which partners from throughout the UK are invited. The feedback from these events is invaluable to LSR and we believe that our partners find it useful to interact with their counterparts from other parts of the country.

Corporate and Social Responsibility
continued

Community Involvement

The success of our business is dependent on the prosperity of the local communities where we own properties. We aim to attract and retain tenants by providing retail accommodation appropriate to their needs in servicing local communities at a price that is in line with the local market and which their business can afford. We are considering initiatives to increase our involvement in local communities and we have recently launched a scheme to supply LSR drinks bottles to local junior sports clubs and school teams.

Environmental Issues

LSR will support initiatives which can lead to sustainable environmental and social benefits. Within our head office we aim to use energy saving devices wherever possible and we have paper and plastic recycling arrangements in place. Fair-trade office supplies are purchased wherever possible. We also try to encourage our staff to travel by public transport or to cycle to the office to reduce our Company carbon footprint.

We believe that our business model encourages people to shop within working distance of their homes, avoiding unnecessary travel and our "local shops, nationwide" philosophy promotes good community relations in which local businesses thrive.

In developing property, LSR focuses on investing in and upgrading existing property stock. It is not our policy to develop new commercial units, thereby minimising construction damage to the environment. Our development projects are, in the main, aimed at extending and improving residential stock above and adjacent to the shops we own. In doing so we supply additional housing stock within existing urban areas, reducing the impact of green field development. All works we undertake comply with relevant building requirements.

We aim to reduce our direct adverse environmental impact by lowering the general energy consumption of our business and using renewable sources of energy wherever possible. We aim to reduce our environmental impact via strong managerial control and informative resources for ourselves and our tenants. In this way we can ensure that the growth of our business is commensurate with our CSR policies. Our policy of engaging local management and agency teams minimises travel and encourages a healthy working relationship with our tenants.

Adrian Dack

Director Private Property Management at NAI Erinaceous based in London

"For the past two and half years I have been the Account Director at NAI-Erinaceous responsible for the LSR account while also directly managing part of the portfolio. The clear strategy set out by LSR greatly assists our day-to-day running of the portfolio and allows us to effectively manage tenant relations. Where decisive action is required we can proceed with their joint support or alternatively negotiate workable solutions with occupiers on their behalf.

Requests for information or instruction are always met in a swift and professional manner and if the properties require works the necessary investment is provided to ensure they are undertaken."

Sustainability

Time: 19:15
Location: **Station Road, Taunton**

"Another long day and I haven't had time to go to the supermarket all week. Luckily there's always the local takeaway by the station. I've got my mates coming over to watch the game, so a few large pizzas should see us through the match. There's no beer in the fridge at home, but I'll have time to pop back around the corner to the off-licence to grab a couple of cans before kick off."

We value the long-term importance of sustaining a local community. By helping to build strong relationships with our tenants and valuing the service they provide, we hope to help support the local area for the future. Changing social trends mean that this specialist market is gaining increasing importance in our daily lives. Diversity of properties in our portfolio allows us to spread the risk of any fluctuations in the market, whilst providing for increasing economies of scale.

Board of Directors

Grahame Whateley

Andrew Cunningham

Nicholas Vetch

Mike Riley

Nick Gregory

Victoria Whitehouse

Grahame Whateley – Independent Non-Executive Chairman

Aged 64, Grahame Whateley, became Chairman of the Company in January 2005, having been involved in the property industry for 45 years. He founded the Castlemore group, of which he is also Chairman, 36 years ago and he is also Chairman of the Cedar group of companies. He serves on the Company's Remuneration and Nomination Committees.

Andrew Cunningham – Senior Independent Non-Executive Director, Chairman of Audit Committee, Chairman of Nomination Committee

Andrew Cunningham, aged 51, joined the Board in May 2007. He qualified as a Chartered Accountant with Deloitte Haskins and Sells, becoming a partner in 1989. He joined Grainger PLC as Finance Director in 1996, becoming Deputy Chief Executive in 2002. Besides chairing the Audit and Nomination Committees, Andrew serves on the Remuneration Committee.

Nicholas Vetch – Independent Non-Executive Director, Chairman of Remuneration Committee

Aged 45, Nick Vetch was joint Chief Executive of Edge Properties, which he co-founded in 1989, before being taken over by Grantchester Properties plc in 1998. In the same year he co-founded Big Yellow Group PLC, where he remains Executive Chairman. He is a Chartered Surveyor and is also a non-executive director of Blue Self Storage S.L., a self storage operation in Spain. Besides chairing the Remuneration Committee, he serves on the Audit Committee.

Mike Riley – Joint Chief Executive Officer

Aged 47, Mike Riley has worked in the property industry since 1986, having trained as a Chartered Surveyor with Hillier Parker. Following this he joined Chesterton International, becoming managing director of its property finance arm, De Groot Collis Financial Services Limited. He joined HBV Real Estate Capital in 1997, becoming joint managing director in 1999. Mike was then at Quintain Estates and Development Plc from July 2001, holding the role of Chief Executive from March 2002. In October 2002 he moved to Castlemore Securities Limited, where he was a director until January 2005, when he became a director of the Company.

Nick Gregory – Joint Chief Executive Officer

Nick Gregory, aged 42, qualified as a Chartered Surveyor having trained at Chesterton from 1993. He then joined UBS Global Asset Management (UK) Limited where he was director responsible for acquisitions for the Triton Property Fund. In October 2002 Nick moved to Castlemore Securities Limited, where he was a director until January 2005, when he became a director of the Company.

Victoria Whitehouse – Finance Director

Aged 34, Victoria Whitehouse trained as a Chartered Accountant with Felton & Co in Birmingham, qualifying in 1997. She then joined KPMG, becoming senior audit manager. In 2005 she moved to ProLogis Developments Limited, where she was Group Financial Controller until January 2007 when she joined the Company, becoming Finance Director in May 2007.

Directors' Report

The directors present their report and audited financial statements of the Group and the Company for the year ended 30 September 2007.

On 16 March 2007 the Company changed its name from Castlemore Capital Limited to The Local Shopping REIT plc.

Group Result and Dividends

The loss for the Group attributable to shareholders for the year was £8.1m (30 September 2006 profit £3.5m). In accordance with the Prospectus issued in April 2007, a final dividend of 3.419p per Ordinary Share was distributed on 3 January 2008 on each of the Ordinary Shares in issue and entitled thereto on 14 December 2007.

Business Review

The business and financial review on pages 10 to 19 constitutes the directors' business review and forms part of this report.

The subsidiary undertakings of the Company are set out in note 24 on page 57.

Acquisitions and Disposals

Information regarding the Group's acquisitions and disposals during the year is set out in note 3 on page 43.

Supplier Payments

The Group has a policy of paying suppliers in accordance with pre-agreed terms.

At 30 September 2007 trade creditors represent an average of 24 days' purchases (2006: 24 days).

Share Capital and Admission to London Stock Exchange

On 11 April 2007, the Company passed resolutions:

- sub-dividing and reclassifying the 600,000 existing issued "A" shares of £1 each into 3,000,000 Ordinary Shares of 20p each;
- sub-dividing and reclassifying the 100,000 existing issued "B" shares of £1 each into 500,000 Ordinary Shares of 20p each;
- sub-dividing and reclassifying the 100,000 existing issued "C" shares of £1 each into 500,000 Ordinary Shares of 20p each;
- increasing the authorised share capital of the Company from £800,000 to £150,000,000 by the creation of 746,000,000 new Ordinary Shares of 20p each;
- adopting new Articles of Association conforming with the requirements for a listed public limited company;
- empowering the directors to issue securities up to an aggregate nominal amount of (i) £18,390,804.60 in connection with the Company's flotation and (ii) an amount equal to one third of the Ordinary Share capital immediately following the allotment of shares pursuant to the Company's flotation, and disapplying the provisions of Section 89 of the Companies Act 1985 in connection with these issues; and
- empowering the directors to purchase up to 14.99% of the Company issued share capital.

All the above resolutions were passed conditional on the Company's admission to the Official List of the London Stock Exchange, to take effect immediately prior to admission.

Pursuant to a placing and offer for subscription the Company issued 91,954,023 Ordinary Shares on 2 May 2007. On the same day the Company was admitted to the Official List of the London Stock Exchange.

On 2 May 2007 the Company allotted 641,521 shares to LSR Trustee Limited, the trustee of the Company's employee benefit trust to cover awards made under the Company's Long Term Incentive Plan.

Cancellation of Share Premium

On 11 May 2007 the Company passed a special resolution cancelling, subject to the sanction of the Court, the amount standing to the credit of its share premium account following the listing of the Company's shares on the London Stock Exchange. This resolution was sanctioned by the Court on 6 June 2007.

REIT Regime

On 10 May 2007 the Company gave notice in the required form to HM Revenue and Customs ("HMRC") that it would enter the UK REIT regime on the following day, this was subsequently acknowledged by HMRC.

Purchase of Shares into Treasury

Monitoring the Company's share price and prevailing market conditions during the final quarter of the year, the directors considered that it would be in the Company's interest for shares to be bought within the market and taken into Treasury and instituted a share buy-back arrangement with the Company's brokers, JPMorgan Cazenove. At 30 September 2007, 2,953,750 Ordinary Shares had been purchased all of which have been taken into treasury (2006: Nil).

Post Balance Sheet Event

Following the year end, share buy-backs described above continued. In view of the Company's close period, this was arranged with an independent third party on the basis of a non-discretionary mandate within pre-set parameters, under which trading decisions were made wholly independently of the Company. Since the year end, 4,000,000 Ordinary Shares have been purchased under this arrangement and all have been taken into treasury. The Company therefore now holds a total of 6,953,750 Ordinary Shares within treasury.

The directors are currently authorised to purchase up to 14.99% of the Company's issued share capital immediately following the Company's admission to the Official List of the London Stock Exchange. The authority will expire at the forthcoming Annual General Meeting when a resolution will be put to shareholders to renew the directors' authority to buy back the Company's shares up to a maximum of 14.99% of the Company's issued share capital at that time.

Charitable and Political Donations

During the year the Group made no donations (2006: £Nil) to charitable organisations. No donations were made for political purposes (2006: Nil).

Directors' Report continued

Directors

The following directors, not having been elected or re-elected at the Company's previous Annual General Meeting, will retire from office at the forthcoming Annual General Meeting in accordance with Article 111 of the Company's Articles of Association and, being eligible, will offer themselves for reappointment:

Andrew Cunningham
Nicholas Gregory
Michael Riley
Nicholas Vetch
Graham Whateley
Victoria Whitehouse

Directors' Interests

No director has any material interest in any contract or arrangement with any company within the Group as at the date of this document which is significant to the activities of the Group.

The interests of the directors in the issued share capital of the Company, all of which were beneficial, are set out below. None of the directors had any beneficial interest in any subsidiaries of the Company.

Director	**30 September 2007**	30 September 2006
Andrew Cunningham	**14,368**	Nil
Nicholas Gregory	**500,000**	100,000*
Michael Riley	**500,000**	100,000*
Nicholas Vetch	**2,873,563**	Nil
Grahame Whateley	**7,660,918**	600,000*
Victoria Whitehouse	**1,149**	Nil

* Prior to the restructuring of the Company's capital on 11 April 2007, described on page 25.

The holdings are all of Ordinary Shares of 20p each. There were no changes of directors' interests in shares between 30 September 2007 and the date of this document.

Directors' interests in employee share schemes are set out on page 31.

Substantial Shareholdings

As at the date of this document the Company had been notified in accordance with Chapter 5 of the Disclosure and Transparency Rules of the following major interests in voting rights attached to its Ordinary Shares of 20p each (which represent interests in 3% or more of its issued ordinary capital excluding shares held in Treasury).

Name	No. of Shares	%
Grahame Whateley	7,660,918	8.19
Fidelity International Limited	7,000,000	7.48
Schroders plc	6,213,792	6.64
AXA S.A.	5,048,350	5.40
Landsdowne Partners Limited & Landsdowne Partners International Limited	4,721,080	5.05
Legal & General Group Plc	3,919,238	4.19
Nicholas Vetch	2,873,563	3.07

Employee Share Schemes

The Company has the following employee share schemes:

The Local Shopping REIT plc Company Share Option Plan ("CSOP")

The CSOP, which was adopted by the Company, with effect from 2 May 2007 and has been approved by HM Revenue & Customs, enables the Remuneration Committee to award options over the Company's shares to any employee of the Company, including executive directors.

The Local Shopping REIT plc Long Term Incentive Plan ("LTIP")

Under the LTIP, which was adopted with effect from 2 May 2007, the awards of Ordinary Shares may be granted to any employee of the Company, including executive directors. Awards are granted at the discretion of the trustee of the Company's Employee Benefit Trust ("EBT"), in consultation with the Remuneration Committee. The EBT maintains a holding of shares from which awards under the LTIP may be sourced.

Employees

Information on the Company's policies towards its employees, including "whistle blowing", ethical standards and employee involvement, is contained in the section on corporate and social responsibility on page 21.

Disclosure to Auditors

So far as the directors are aware, there is no information relevant to the Auditors' preparation of their report that has not been disclosed to the Company's Auditors. Each director has taken all steps required of a director to ensure that he/she is aware of any information relevant to the audit and to establish that all such information has been disclosed to the Auditors.

Annual General Meeting

The Annual General Meeting of the Company will be held on 27 February 2008 at KPMG LLP, Floor 39, One Canada Square, Canary Wharf, London E14 5AG, beginning at 11.00am.

Auditors

During the year KPMG LLP resigned as Auditors and the directors appointed KPMG Audit Plc.

KPMG Audit Plc have indicated that they are willing to continue as Auditors to the Company and a resolution proposing their re-appointment will be put to the forthcoming Annual General Meeting.

This report was approved by the directors on 11 January 2008.

W A Heaney
Company Secretary

11 January 2008

Corporate Governance

Compliance With the Combined Code

The Company was admitted to the Official List of the London Stock Exchange on 2 May 2007, since when it has complied with the provisions of section 1 of the Combined Code on Corporate Governance ("the Combined Code"). This statement summarises how the principles set out in the Combined Code have been implemented.

Effective Board, Collectively Responsible for the Success of the Company

The Board meets regularly to review the Company's operations and success in putting its investment strategy in effect. Whilst day-to-day operational management is delegated to the executive directors, the Board maintains responsibility for overall strategy and major investment decisions. The non-executive directors make themselves available to provide guidance to the management team on operational issues based on their experience.

Division of Responsibilities

There is a clear division of responsibilities between executive and non-executive directors, with the Chairman's remit clearly separate from that of the joint Chief Executives. Rules are in place to identify those items that should be referred to the Board as a whole. The functions of the Board's committees are set out in terms of reference approved by the Board and each non-executive director's duties and obligations are clearly set out in his letter of appointment.

Balance

The Board considers that its composition of three independent non-executive directors and three executive directors conforms to the requirement for balance and the need to avoid domination of decision taking. Although the Company's Chairman, Grahame Whateley, was a major investor in the Company during its infancy and prior to its Stock Exchange flotation, the Board considers that this has no bearing on Mr Whateley's present chairmanship of the Company and that he should be regarded as independent for the purposes of the Combined Code.

Board Meetings and Information

Each Board meeting has a formal agenda, with key items reviewed on a regular basis. In consultation with the Chairman, the Company Secretary ensures that all directors receive up-to-date and accurate reports and summaries prior to each meeting. Outside the Board meeting cycle, directors receive month-end progress reports and key management information.

Performance Evaluation

In view of the relatively short time that has elapsed since the Company's Stock Exchange flotation, the Board has not fully implemented the performance review principles set out in the Combined Code. However, future reports will comment on the conduct of this process.

Board Appointments

The Board has established a Nomination Committee, which is responsible for ensuring that all appointments meet the required standards of skills, experience and stewardship ability in accordance with the principles of the Combined Code.

The Company's Articles of Association require any director appointed to the Board during the year to be reappointed at the next Annual General Meeting. One-third of the remaining directors must also retire and offer themselves for reappointment.

Remuneration

The Board took independent advice before setting the level of remuneration for its non-executive directors. The Remuneration Committee also considered advice from independent consultants in deciding on the remuneration and reward schemes applicable to the executive directors and senior managers.

Board Committees: Audit Committee

The Audit Committee was instituted when the Company was admitted to the Official List of the London Stock Exchange in May 2007. The Committee's chairman is Andrew Cunningham and its other member is Nicholas Vetch. Their biographical details are set out on page 24. As Deputy Chief Executive and Finance Director of Grainger PLC, Andrew Cunningham was considered by the Board to have the requisite skills to chair the Committee. The Committee has formal terms of reference approved by the Board. Committee meetings may be attended, by invitation, by other members of the Board. The Company's Auditors, KPMG Audit Plc, attend most of the Committee's meetings and the Committee has the opportunity to meet the Auditors in the absence of the executive directors and members of the management team. The Committee met once during the year to 30 September 2007.

The Company Secretary acts as secretary to the Committee.

Whistle Blowing Arrangements

Procedures for internal "whistle blowing" are covered in the section on corporate and social responsibility on page 21.

KPMG Non-Audit Work

In order to safeguard the objectivity of the Company's Auditors, strict procedures have been put in place for the engagement of KPMG in non-audit work. Careful consideration is given to whether such work might give rise to a conflict of interest and the Chairman of the Audit Committee must separately authorise any item of work for which the fee is in excess of 50% of the audit fee in any year.

Board Committees: Remuneration Committee

Full details of the membership of the Remuneration Committee are set out in the Directors' Remuneration Report on pages 29 to 32. The Committee met once during the year. Each member attended all the meetings.

Corporate Governance continued

Board Committees: Nomination Committee

The Nomination Committee comprises at least three directors, the majority of whom are independent non-executive directors. The committee is chaired by the senior independent non-executive director (other than the Chairman), Andrew Cunningham. As the Committee was established during the latter half of the financial year, it did not meet during the year. Under the Committee's terms of reference it will meet at least once during each financial year, usually during the quarter prior to the Annual General Meeting.

Investor Relations

The Company has a programme of meetings with its shareholders, usually involving the Joint Chief Executive Officers. Those involved report on these meetings to the Board, together with general feedback from investors and the Company's bankers and advisers. The Board intends to make full use of the Annual General Meeting as an opportunity for dialogue with shareholders and the Company's website is kept up to date with major activities and developments.

Director Induction

Each of the Company's non-executive directors received an induction session and pack. The Company also made arrangements for non-executive directors to visit its sites. Non-executive directors are welcome to visit the Company's offices and (by arrangement with tenants) its investment properties at any time.

Accountability and Audit

Going Concern

After due enquiry the directors have a reasonable expectation that the Company and the Group has sufficient resources to continue operating for the foreseeable future. Accordingly, the financial statements have been prepared on a going concern basis.

Internal Controls

The directors acknowledge their responsibility for establishing an appropriate system of internal controls and monitoring its effectiveness. The system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatements or loss. Terms of reference are in place covering the responsibilities of the Board's committees. The Board has delegated authority to the executive directors. However, clear statements are in place identifying those matters which the Board has reserved to itself for decision and matters on which the executive directors are expected to consult the Board. The Board thereby retains control over corporate strategy, annual budgets, significant contracts outside the ordinary course of business and corporate acquisitions and disposals. There are prescribed limits to the executive directors' authority to commit the Company to expenditure and borrowing.

The Audit Committee is responsible for reviewing the Company's risk identification and internal control systems. Following the 30 September 2007 year end, the Committee has reviewed the findings of the Company's auditors and insurance brokers, as well as the views of the Company's operational managers. In addition, the members of the Audit Committee monitor the effectiveness of the Company's risk and control systems on an informal basis throughout the year, bringing to bear their knowledge and experience of the ways in which these matters are handled in other listed companies. The Company's approach to these matters, summarised below, is considered to accord with the principles of the "Turnbull Guide" – Internal Controls: Guidance for Directors on the Combined Code. This approach covers all companies within the Group and there are no associate or joint venture entities which it does not cover.

Control Environment and Procedures

The Group's established internal control process comprises:

- top-level risk identification, evaluation and management framework monitored by the Audit Committee;
- written remits for executive management identifying items reserved to the Board and its committees;
- a procedures manual covering all operational activity, including limits of authority and authorisation procedures;
- effective systems for authorising capital expenditure and recording actual cost incurred;
- systematic induction process for all joiners and ongoing staff development;
- regular team meetings to identify operational developments and processes to be put in place to deal with them effectively;
- established procedures for electronic information control and security;
- regular independent audits;
- regular operational and individual performance reviews by executive management;
- monthly reporting to the Board of operational results against expectations with commentary on variances;
- regular review of operational forecasts and consideration by the Board on a quarterly basis;
- regular review of the Company's funding requirements against the status of the financial markets and the ongoing effectiveness of the Company's hedging arrangements; and
- quarterly reporting of health, safety and environmental matters.

Directors' Remuneration Report

This report covers:

- the establishment and remit of the Remuneration Committee;
- the Company's policy for the remuneration of its directors for the year ended 30 September 2007 and, subject to shareholder approval, subsequent financial years; and
- details of the directors' remuneration packages and contracts.

Remuneration Committee

The Remuneration Committee ("the Committee") is responsible for:

- determining the broad policy for the remuneration and benefits of the Company's executive directors and senior managers;
- approving the design and performance targets for share-related performance plans for the Company; and
- determining individual remuneration packages of each director, giving due regard to the provisions and recommendations of the Combined Code and the Listing Rules.

The Committee has met twice during the year. The Committee comprises solely of independent non-executive directors. The following directors serve on the Committee:

Nicholas Vetch (Committee Chairman)
Andrew Cunningham
Grahame Whateley

Biographical details of the members of the Committee are set out on page 24.

Other than the Company Secretary, who serves as secretary to the Committee, other directors or executives attend meetings of the Committee only by invitation and none did so during the year. In setting the remuneration packages of the executive directors and establishing the Company's share-related incentive plans, the Committee received independent advice on executive remuneration from New Bridge Street Associates, remuneration consultants. New Bridge Street Associates does not provide any other services to the Group.

Remuneration Policy

The Company's remuneration policy is based on the following principles:

- within a competitive market, retaining and facilitating the recruitment of individuals whose talent matches the entrepreneurial and leadership needs of the business, enabling the Company to fulfil its investment objectives for its shareholders; and
- placing emphasis on performance-related rewards and focusing on incentive targets that are closely aligned with the interests of shareholders.

The mix of basic pay, benefits, annual bonus and long-term awards contained in the remuneration packages adopted for the executive directors reflect these principles. The approach adopted by the Committee is to set base pay and other fixed remuneration at less than the median for companies in the FTSE real estate sector. By the same token, total remuneration including performance-based awards is aimed at between the median and upper quartile relative to the sector. However, rewards at this level will only be generated provided the executives achieve stretching performance targets.

Base Pay and Benefits

Basic salary and benefits are reviewed annually by the Committee against comparable market groups. In addition to their base salary, the executive directors are provided with private health insurance and death in service and disability insurance cover.

Directors' Pensions

The Company has established a Stakeholder Pension Plan which all employees, including executive directors, are eligible to join. No executive director is a member of this pension plan at the date of this document.

With effect from 2 May 2007 the Company made contributions to the personal pension plans of executive directors, as a percentage of base salary, as follows:

Nicholas Gregory	10% per annum
Michael Riley	10% per annum

Annual Executive Bonus Plan

The Committee has adopted an Annual Executive Bonus Plan ("the bonus plan") that makes bonus payments to the participants to the extent that performance targets set by the Committee are achieved during the financial year. Under the bonus plan the Joint Chief Executives may earn annual awards of up to 100% of base salary and the Finance Director may earn bonus awards of up to 50% of salary. The maximum bonus for other participating executives will be determined by the Committee, but will not exceed 100% of base salary.

The first performance period for the bonus plan runs from 2 May 2007 (the date of the Company's admission to the Official List of the London Stock Exchange) to 30 September 2008. Accordingly, no payment will be made under the plan purely in respect of the year ended 30 September 2007. Thereafter the performance period will ordinarily be the Company's financial year.

For the first performance period bonuses will be payable dependent on the extent by which the total property return for the Company during the performance period exceeds that of the Investment Property Databank Index for Standard Shops during the same period.

It is the Committee's intention that for the year ended 30 September 2009 and subsequent performance periods 50% of any bonus payable under the bonus plan will depend on the Company's total property return, as described above, with the remaining 50% dependent on the growth in the Company's Dividend Per Share in comparison with the growth in the Consumer Price Index during the performance period.

Long Term Incentive Plan

The Company's Long Term Incentive Plan ("the LTIP") came into force on the Company's admission to the Official List of the London

Directors' Remuneration Report
continued

Stock Exchange on 2 May 2007. Under the terms of the LTIP employees, including executive directors, may be granted awards of the Company's shares in the form of a nil cost option. The LTIP is operated by the Committee in conjunction with the Company's Employee Benefit Trust ("EBT"), which may grant awards on the Committee's recommendation.

The exercise of awards granted under the LTIP is conditional on the achievement of objective performance targets set by the Committee at the time of grant. Performance is measured over a minimum period of three years and awards may not be exercised until after the expiry of the relevant performance period. The first awards under the LTIP were made at the Company's admission to the Official List of the London Stock Exchange on 2 May 2007 and the performance period runs to 2 May 2010. Under these initial awards, 50% of the shares subject to the award are subject to the satisfaction of an Absolute TSR target. Under this target:

- no award may be exercised in respect of the shares subject to the Absolute TSR target if the average annual percentage growth in the Company's Total Shareholder Return over the performance period is less than 8%;
- an award may be exercised as to 20% of the shares subject to the Absolute TSR target if the average annual percentage growth in the Company's Total Shareholder Return over the performance period is equal to or greater than 8%;
- an award may be exercised as to 100% of the shares subject to the Absolute TSR target if the average annual percentage growth in the Company's Total Shareholder Return over the performance period is equal to or greater than 16%; and
- where the Company achieves a Total Shareholder Return over the performance period of between 8% and 16%, the award may be exercised on a pro rata basis between 20% and 100% of the shares subject to the Absolute TSR target.

The remaining shares under the award are subject to a Comparator TSR target. Under this the Company's Total Shareholder Return is compared with a comparator group of publicly quoted real estate investment companies, and by which:

- no award may be exercised in respect of the shares subject to the Comparator TSR target unless the Company is ranked equal to or above the 50th percentile by reference to its Total Shareholder Return relative to that of the comparator group over the performance period;
- an award may be exercised as to 25% of the shares subject to the Comparator TSR target if the Company is ranked equal to the 50th percentile by reference to its total shareholder return relative to that of the comparator group over the performance period; and
- an award may be exercised as to a further 3% of the shares subject to the Comparator TSR target for each percentile by which the Company is ranked above the 50th percentile, so that the award subject to the Comparator TSR target may be capable of exercise in full if the Company is ranked equal to or above the 75th percentile.

The LTIP is subject to an overriding exercise requirement, under which no award may be exercised unless the Company has complied with the REIT regulations in relation to dividend distribution throughout the performance period.

Employee Share Option Plan

The Local Shopping REIT plc Company Share Option Plan ("the CSOP") came into force on the Company's admission to the Official List of the London Stock Exchange on 2 May 2007, at which time the CSOP was formally approved by HM Revenue & Customs. The CSOP is operated by the Committee and, under the terms of the CSOP, employees of the Company, including executive directors, are eligible to be granted options over the Company's shares at the Committee's discretion. The exercise price of options granted under the CSOP will not normally be less than the market value of the shares on the dealing day immediately prior to the date of grant. The exercise of options will not normally be subject to a performance target. Options may ordinarily be exercised between the third and tenth anniversary of their grant. To date no awards have been made to executive directors under the CSOP.

Internal Relativity

The Committee is sensitive to the need to set directors' remuneration having regard to pay and conditions generally within the Company and for the Company to remain competitive as an employer within the sector and will continue to monitor internal and external relativities in line with the Company's growth and the evolving market.

Non-Executive Directors

The level of fees paid to non-executive directors was set at the time of the Company's admission to the Official List of the London Stock Exchange having regard to market levels at that time. The level of non-executive pay will be reviewed at least every three years by the Chairman and the executive directors, to whom the Board have delegated this task.

Terms of Appointment

In accordance with the Company's Articles of Association, the appointments of all the Company's directors are due for ratification at the forthcoming Annual General Meeting. The directors will then be subject to retirement by rotation at future Annual General Meetings.

For non-executive directors, the Company's policy is for initial appointments to be for a term of three years, subject to termination on notice by the Company or the director. Letters of appointment are in place in all cases and set out the expected time commitment of the non-executive directors to the Company's affairs.

For executive directors, the Company's policy is that service contracts should be capable of termination by the Company at not more than one year's notice. The Company has the right to terminate the service contracts without full notice on the payment of compensation in lieu of the period of notice foregone.

Save as indicated below, the remainder of this report has been audited.

Directors' Total Emoluments

Non-Executive Directors

Director	Salary or Fee £	Bonus £	Benefits in Kind £	**Total 2007 £**	Total 2006 £
Grahame Whateley	23,004	–	–	**23,004**	–
Andrew Cunningham	13,691	–	–	**13,691**	–
Nicholas Vetch	13,691	–	–	**13,691**	–
Executive Directors					
Nicholas Gregory	247,966	–	11,260	**259,226**	179,067
Michael Riley	304,266	–	11,237	**315,503**	270,784
Victoria Whitehouse	105,122	–	111	**105,233**	–
Total	707,740	–	22,608	**730,348**	449,851

Pension contributions of £21,667 (2006: £Nil) have been made to certain directors' personal pension schemes and are included in benefits in kind.

Directors LTIP Awards

Director	Shares Subject to Award at 1 October 2006	Granted During the Year	Exercised During the Year	Lapsed During the Year	**Shares Subject to Award at 30 September 2007**	Market Value Per Share at Award Date	Exercise Dates From	To
Nicholas Gregory	Nil	298,850	Nil	Nil	**298,850**	1.74	3 May 2010	1 May 2017
Michael Riley	Nil	298,850	Nil	Nil	**298,850**	1.74	3 May 2010	1 May 2017
Victoria Whitehouse	Nil	16,522	Nil	Nil	**16,522**	1.74	3 May 2010	1 May 2017
Total	Nil	614,222	Nil	Nil	**614,222**			

Directors' Service Contracts

The following tables summarise the directors' service contracts or terms of appointment:

Non-Executive Directors

Director	Date of Appointment as a Director	Date of Current Appointment Letter	Expiry of Term
Grahame Whateley	20 December 2004	30 March 2007	29 March 2008
Andrew Cunningham	30 March 2007	30 March 2007	29 March 2008
Nicholas Vetch	30 March 2007	30 March 2007	29 March 2008

Executive Directors

Director	Date of Contract	Notice Period
Nicholas Gregory	30 March 2007	12 months from either party
Michael Riley	30 March 2007	12 months from either party
Victoria Whitehouse	30 March 2007	12 months from either party

Directors' Remuneration Report
continued

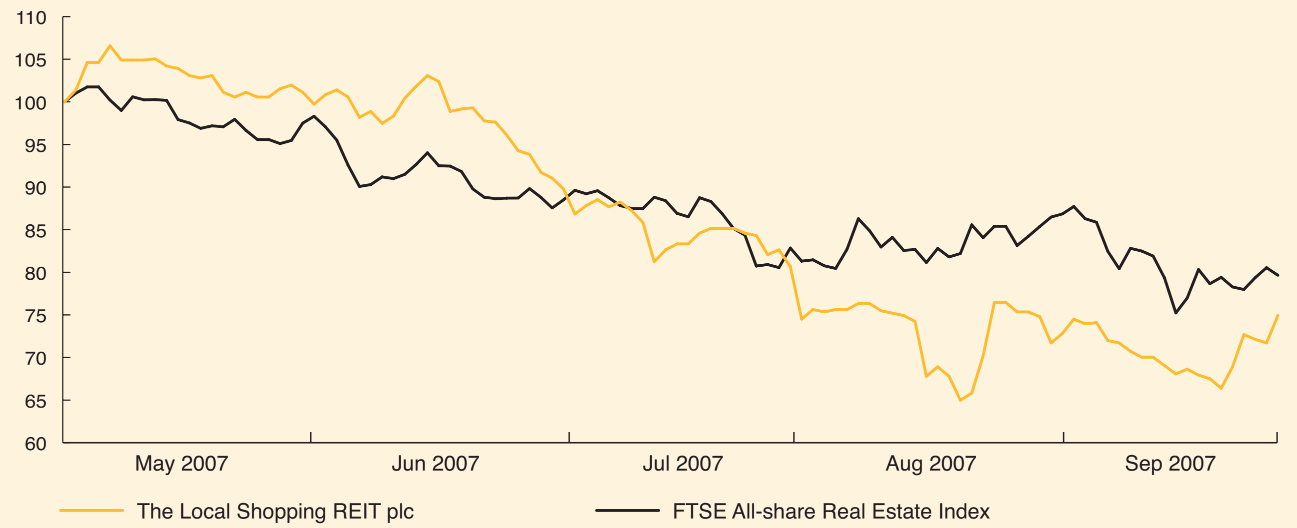
External Appointments

The non-executive directors consider it beneficial in principle for the Company for the executive directors to hold a limited number of outside directorships or other appointments. However, it is considered that such appointments are not appropriate whilst the Company remains in its early growth stage. It has therefore been agreed that the executive directors will not be entitled to take up any external non-executive appointments until after the elapse of two years from the Company's admission to the Official List of the London Stock Exchange, at which time they will be entitled to take up one non-conflicting appointment. Any further appointments will be subject to approval by the Board.

Performance Graph (Not Audited)

TSR Performance from IPO on 2 May 2007 to 30 September 2007

Source: Thomson Datastream



The Total Shareholder Return ("TSR") performance graph above sets out the comparison of the Company's TSR against the Real Estate Sector. This comparison has been chosen as it is considered the most appropriate benchmark against which to assess relative performance of the Company.

This report has been approved by the Board of directors.

N Vetch
Remuneration Committee Chairman

11 January 2008

Statement of Directors' Responsibilities In Respect of the Annual Report and 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 Group and parent company financial statements for each financial year. Under that law 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 law (UK 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 and of the profit or loss of the parent company for that period.

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.

Under applicable law and regulations, the directors are also responsible for preparing a Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that comply with that law and those regulations.

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.

Independent Auditors' Report to the Members of Local Shopping REIT plc

We have audited the Group and parent company financial statements (the "financial statements") of The Local Shopping REIT plc for the year ended 30 September 2007 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. We have also audited the information in the Directors' Remuneration Report that is described as having been audited.

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 and the Directors' Remuneration Report 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 33.

Our responsibility is to audit the financial statements and the part of the Directors' Remuneration Report to be audited 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 and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985 and as regards the Group financial statements, Article 4 of the IAS Regulation. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements. The information given in the Directors' Report includes that specific information presented in the Financial Review that is cross referenced 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 review whether the Corporate Governance Statement reflects the Company's compliance with the nine provisions of the 2006 Combined Code specified for our review by the Listing Rules of the Financial Services Authority, and we report if it does not. We are not required to consider whether the board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's Corporate Governance procedures or its risk and control procedures.

We read 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.

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 and the part of the Directors' Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the 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 financial statements and the part of the Directors' Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Directors' Remuneration Report to be audited.

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 September 2007 and of its loss for the year then ended;
- the Group financial statements have been properly prepared in accordance with the Companies Act 1985 and Article 4 of the IAS Regulation;
- 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 September 2007;
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

KPMG Audit Plc, Birmingham
Chartered Accountants
Registered Auditor

11 January 2008

Consolidated Income Statement

for the year ended 30 September 2007

	Note	Year Ended 30 September 2007 £000	Year Ended 30 September 2006 £000
Gross rental income		**13,101**	5,528
Property operating expenses		**(1,642)**	(420)
Net rental income	4	**11,459**	5,108
Profit/(loss) on disposal of investment properties		**83**	(47)
(Loss)/gain from change in fair value of investment properties		**(6,424)**	5,054
Administrative expenses	5	**(2,573)**	(1,084)
Net other income	6	**25**	477
Operating profit before goodwill and net financing costs		**2,570**	9,508
Negative goodwill arising on acquisition	3	**2,046**	–
Operating profit before net financing costs		**4,616**	9,508
Financing income	7	**1,302**	1,130
Financing expenses	7	**(10,180)**	(5,921)
Operating (loss)/profit after financing costs		**(4,262)**	4,717
Result of joint venture	11	**–**	–
(Loss)/profit before tax		**(4,262)**	4,717
Taxation	8	**(3,799)**	(1,179)
(Loss)/profit for the year attributable to equity holders of the Company	18	**(8,061)**	3,538

Basic and diluted (loss)/earnings per share	19	**(20.0)p**	166.6p

Consolidated Balance Sheet

as at 30 September 2007

	Note	At 30 September 2007 £000	At 30 September 2006 £000
Non-current assets			
Plant and equipment	9	**73**	–
Investment properties	10	**247,608**	141,539
Investment in joint ventures	11	**–**	–
Deferred tax asset	12	**–**	991
Derivative financial instruments	20	**1,034**	772
Total non-current assets		**248,715**	143,302
Current assets			
Derivative financial instruments	20	**553**	369
Trade and other receivables	13	**4,829**	3,563
Investment properties held for sale	10	**3,081**	–
Cash		**5,735**	2,891
Total current assets		**14,198**	6,823
Total assets		**262,913**	150,125
Non-current liabilities			
Interest bearing loans and borrowings	15	**(98,149)**	(136,583)
Deferred tax liabilities	12	**–**	(1,776)
Derivative financial instruments	20	**–**	(70)
Finance lease liabilities	17	**(1,353)**	(618)
Total non-current liabilities		**(99,502)**	(139,047)
Current liabilities			
Bank overdraft	14	**(115)**	(91)
Interest bearing loans and borrowings	15	**–**	(3,231)
Trade and other payables	16	**(11,523)**	(4,387)
Total current liabilities		**(11,638)**	(7,709)
Total liabilities		**(111,140)**	(146,756)
Net assets		**151,773**	3,369
Equity			
Issued capital	18	**20,098**	800
Share premium	18	**–**	–
Reserves	18	**3,773**	31
Retained earnings	18	**127,902**	2,538
Total attributable to equity holders of the Company		**151,773**	3,369

The financial statements were approved by the Board of directors and authorised for issue on 11 January 2008. They were signed on its behalf by:

M E Riley
Joint CEO

N J Gregory
Joint CEO

Consolidated Statement of Cash Flows

for the year ended 30 September 2007

	Note	**Year Ended 30 September 2007 £000**	Year Ended 30 September 2006 £000
Operating activities			
(Loss)/profit for the year		**(8,061)**	3,538
Adjustments for:			
Losses/(gains) on fair value adjustment of investment properties		**6,424**	(5,054)
Net interest expense		**8,878**	4,791
(Profit)/loss on disposal of investment properties		**(83)**	47
Negative goodwill arising on acquisition		**(2,046)**	–
Income tax expense		**3,799**	1,179
		8,911	4,501
Increase in trade and other receivables		**(1,175)**	(2,566)
Increase in trade and other payables		**1,058**	2,251
		8,794	4,186
Interest paid		**(8,225)**	(4,815)
Interest received		**786**	90
Net cash from operating activities		**1,355**	(539)
Investing activities			
Acquisition of subsidiary, net of cash acquired	3	**(6,700)**	–
Proceeds from sale of investment properties		**1,139**	1,805
Acquisition of investment properties		**(101,289)**	(117,892)
Cash flows from investing activities		**(106,850)**	(116,087)
Financing activities			
Proceeds from the issue of share capital		**153,150**	–
Repayment of borrowings		**(251,966)**	(1,317)
New borrowings		**207,023**	120,505
Payment of finance lease liabilities		**108**	49
Cash flows from financing activities		**108,315**	119,237
Net increase in cash		**2,820**	2,611
Cash at 1 October 2006		**2,800**	189
Cash at 30 September 2007	14	**5,620**	2,800

Consolidated Statement of Recognised Income and Expense

for the year ended 30 September 2007

	2007 £000	2006 £000
Net income recognised directly in equity	**–**	–
(Loss)/profit for the year	**(8,061)**	3,538
Total recognised income and expense for the year attributable to equity holders of the Company	**(8,061)**	3,538

Notes to the Financial Statements

for the year ended 30 September 2007

1 Accounting Policies

Basis of Preparation

The Local Shopping REIT plc ("the Company") is a company incorporated and domiciled in the UK. On 16 March 2007 the Company changed its name from Castlemore Capital Limited to The Local Shopping REIT plc and re-registered as a public company, formerly it was registered as a private company.

The Group's financial statements have been prepared in accordance with International Accounting Standards ("IFRS") as adopted by the EU and in accordance with the provisions of the Companies Act 1985.

The Company and its subsidiaries have previously prepared company accounts in accordance with UK Generally Accepted Accounting Practices which were not consolidated. Following admission to the London Stock Exchange, in common with all companies listed on European Regulated markets, the Group is now required to prepare consolidated financial statements in accordance with IFRS. The Company took account of the requirements of IFRS 1 (First Time Adoption of IFRS) in the Prospectus issued prior to the flotation where it presented a reconciliation between UK GAAP and IFRS for the period to 30 September 2006. The Prospectus remains available on the Company's website.

These financial statements are prepared in pounds sterling, rounded to the nearest thousand. They have been prepared under the historical cost convention except for the following assets which are measured on the basis of fair value: investment properties, derivatives and investment properties held for sale.

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

Basis of Consolidation

The consolidated financial statements include the financial statements of the Company and all its subsidiary undertakings up to 30 September 2007. Subsidiaries are consolidated from the date on which the Group obtains control, being the power to govern the financial and operating policies of the entity so as to obtain benefit from its activities. They continue to be consolidated until the date that such control ceases. The financial statements of subsidiaries are prepared using consistent accounting policies. Inter company transactions and balances are eliminated.

Joint ventures are those entities over whose activities the Group has joint control, established by a contractual agreement. The consolidated financial statements include the Group's share of the total recognised gains and losses of jointly controlled entities on an equity accounted basis. Any losses will be restricted to Nil where there is no legal or constructive obligation for the Group to make payments to settle any of the joint venture's liabilities.

Goodwill

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

Investment Property

Investment properties are those properties owned by the Group that are held to earn rental income or for capital appreciation or both and are not occupied by the Company or any of its subsidiaries.

The fair value of investment properties are based on market values being an estimated amount for which a property could be exchanged on the date of valuation under an arm's length transaction between a willing buyer and seller after proper marketing wherein the parties had acted knowledgably, prudently and without compulsion. Professional external valuers have valued a sample selected by themselves of 25% of the existing portfolio and all new purchases since the previous valuation to the year end. The remainder of the portfolio has been valued at its fair value at the year end by the directors who have appropriate recognised professional qualifications and recent experience of the location and category of the property being valued.

Notes to the Financial Statements

for the year ended 30 September 2007

1 Accounting Policies continued

Investment properties are treated as acquired at the point the Group assumes the significant risks and returns of ownership. Subsequent expenditure is charged to the asset's carrying value only when it is probable that future economic benefits associated with the expenditure will flow to the Group and the cost of each item can be reliably measured. All other repairs and maintenance costs are charged to the income statement during the period in which they are incurred.

Disposals of investment properties are recognised on completion; profits and losses arising are recognised through the income statement, the profit is determined as the difference between the sales proceeds and the carrying amount of the asset at the commencement of the year plus any additional expenditure incurred in the year.

Interest on loans associated with acquiring investment properties is expensed on an accruals basis.

Rental income from investment properties is accounted for as described below.

Investment Properties Held for Sale

Investment properties held for sale are included in the balance sheet at their fair value.

Head Leases

Where a property is held under a head lease and is classified as an investment property, it is initially recognised as an asset based on the sum of the premium paid on acquisition and the net present value of the minimum ground rent payments. The corresponding rent liability to the leaseholder is included in the balance sheet as a finance obligation in current and non-current borrowing. On payment of a ground rent the head lease is allocated between liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The interest element of the finance lease is charged to the income statement and the balance reduces the liability.

Plant and Equipment

All plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure which is directly attributable to the acquisition of the asset.

Depreciation is charged to the income statement on the following basis:

- Fixtures and fittings – 15% reducing balance; and
- Computer equipment – straight line basis over three years.

Trade and Other Receivables

Trade and other receivables are initially recognised at fair value and subsequently held at amortised cost less impairment. Impairment is made where it is established that there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivable. The impairment is recorded in the income statement.

Cash and Cash Equivalents

Cash and cash equivalents comprise cash balances and deposits held on call. Cash equivalents are short-term, highly liquid investments with original maturities of three months or less. Bank overdrafts that are repayable on demand are included within cash and cash equivalents for the purpose of the cash flow statement.

Derivative Financial Instruments and Hedging

The Group uses derivative financial instruments such as interest rate swaps to hedge risks associated with interest rate fluctuations. The Group does not hold or issue derivatives for trading purposes.

Such instruments are initially measured at fair value on the date on which a contract is entered into and are subsequently re-measured at fair value.

The Group has determined that the derivative financial instruments did not qualify as effective for hedge accounting under the criteria set out in IAS 39 and consequently any gains or losses arising from changes in their fair value are taken to the income statement. In the future and on an ongoing basis as new derivative financial instruments are entered into, the directors will review the derivative contracts to consider whether they qualify for hedge accounting.

1 Accounting Policies continued

Financial Assets

The Group's policy is to impair financial assets only when there is objective evidence that the cash flows from the financial asset are reduced.

Trade and Other Payables

Trade and other payables are initially recognised at fair value and subsequently held at amortised cost less impairment.

Ordinary Share Capital

External costs directly attributable to the issue of new Shares are shown in equity as a deduction from the proceeds.

Shares which have been repurchased are classified as Treasury Shares and shown in retained earnings. They are recognised at the trade date for the amount of consideration paid, together with directly attributable costs. This is presented as a deduction from total equity.

Rental Income

Rental income from investment properties leased out under operating leases is recognised in the income statement on a straight line basis over the term of the lease. When the Group provides lease incentives to its tenants the cost of incentives are recognised over the lease term, on a straight line basis, as a reduction to income.

Other Income

Other income includes property management fees which are recognised in the income statement on the basis of work done and insurance commission which is recognised over the term of the premium it relates to.

Taxation

Corporation tax on the profit or loss for the year comprises current and deferred tax. Corporation tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the balance sheet date and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method. Provision is made for temporary differences between the carrying amounts of assets and liabilities in the financial statements for financial reporting purposes and the amounts used for taxation purposes. Deferred income tax is calculated after taking into account any indexation allowances and capital losses on an undiscounted basis. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities using tax rates enacted or substantially enacted at the balance sheet date. Deferred tax assets are recognised only to the extent that it is probable that future profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised. Deferred tax assets and liabilities are only offset if there is a legally enforceable right of set off.

Share-Based Payments

The Group operates equity settled, share-based compensation plans comprising awards under a Long Term Incentive Plan ("LTIP") and a Company Share Option Plan ("CSOP") for certain employees. The fair values of these schemes are measured at their fair value at the date of grant. The fair value is then recognised as an employee cost, with a corresponding increase in equity, on a straight line basis over the vesting period, based on the Group's estimate of the shares that will eventually vest.

The fair value of each scheme is measured using an option pricing model. The awards under the LTIP scheme are measured using a Monte Carlo simulation model and the awards under the CSOP scheme are measured using a Black Scholes model.

Notes to the Financial Statements

for the year ended 30 September 2007

1 Accounting Policies continued

Use of Estimates and Judgements

To be able to prepare accounts according to generally accepted accounting principles, management must make estimates and assumptions that affect the asset and liability items and revenue and expense amounts recorded in the financial accounts. These estimates are based on historical experience and various other assumptions that management and the Board of Directors believe are reasonable under the circumstances. The results of these considerations form the basis for making judgements about the carrying value of assets and liabilities that are not readily available from other sources.

The areas requiring the use of estimates and judgements that may significantly impact the Group's earnings and financial position include the estimation of the fair value of investment properties and derivative financial instruments.

The valuation of the Group's investment properties is the main area of judgement exercised by the Board in respect of the Group's results. The Board have relied upon an external valuation carried out by professionally qualified valuers in accordance with the Appraisal and Valuation Standards of the Royal Institute of Chartered Surveyors in respect of all properties purchased since 28 March 2007 and a further 25% of the portfolio as selected by the valuers. These valuers were acting as independent valuers and have good information and experience of the current market prices for properties similar to those owned by the Group. The remainder of the portfolio has been valued by the directors on the same basis.

The valuation of derivative financial instruments and the fixed rate loan are also areas where judgement has been exercised by the Board. These assets and liabilities have been valued by JC Rathbone Associates Limited and this valuation has been relied upon by the Board.

New Standards and Interpretations Not Yet Adopted

There are a number of new standards, amendments to standards and interpretations of standards which are not yet effective for the year ended 30 September 2007 and have not been applied in preparing these consolidated financial statements. They are as follows:

- IFRS 7 – Financial Instruments: Disclosures and the related amendment to IAS 1 on capital disclosures was in issue at the year end. IFRS 7 will require additional disclosure on financial instruments when it comes into effect for the year commencing 1 October 2007 but is not expected to have any material impact on the financial position of the Company;

- IFRS 8 – Operating Segments adopts the "management approach" to segmental reporting which requires the disclosure of segmental information based on internal reports regularly reviewed by the CEO in order to assess each segment's performance. The Group currently operates a single business segment given the wide diversity of the property portfolio held but will reconsider this at the next financial year end; and

- The revised standard IAS 23 – Borrowing Costs removes the option to expense borrowing costs and requires the capitalisation of borrowing costs directly attributable to acquisition, construction and production of a qualifying asset as part of the cost of that asset. However, the standard does not have to be applied to qualifying assets measured at fair value. Therefore, upon adoption, the revised standard is not expected to have a material impact on the Group's financial statements.

The adoption of IFRIC 12 – Service Concession Arrangements, IFRIC 13 – Customer Loyalty Programmes and IFRIC 14 – The Limit on a Defined Benefit Asset Minimum Funding Requirements are not expected to have any effect on the Group's financial statements.

2 Segmental Reporting

The Group operates a single business segment providing accommodation to rent across the United Kingdom. The Group's net assets, revenue and profit before tax are attributable to this one activity.

3 Acquisitions of Subsidiaries

On 29 August 2007, the Group acquired the entire share capital of Gilfin Property Holdings Limited for a combination of cash and the issue of new equity. The Company holds a portfolio of properties located in Scotland and London.

The acquisition had the following effect on the Group's assets and liabilities on acquisition date:

	Pre-Acquisition Carrying Amounts £000	Fair Value Adjustments £000	Values Recognised on Acquisition £000
Property	14,606	–	14,606
Trade and other receivables	91	–	91
Cash and cash equivalents	135	–	135
Trade and other payables	(423)	–	(423)
Loans and borrowings	(1,008)	–	(1,008)
Net identifiable assets and liabilities	13,401	–	13,401
Consideration paid			
Cash paid including costs of acquisition*			(6,835)
Fair value of new equity issued			(4,520)
Negative goodwill arising on acquisition			2,046
Cash acquired			135
Cash consideration			(6,835)
Net cash outflow			(6,700)

* including costs associated with the acquisition of £330,000 and a further payment of £80,000 following settlement of the completion accounts.

Pre-acquisition carrying amounts were determined based on applicable IFRSs immediately prior to the acquisition. The values of assets, liabilities and contingent liabilities recognised on acquisition are their fair values.

The fair value of the assets acquired was in excess of the consideration given of £12.85m as the number of shares issued (3,897,246) was based on the net asset value per share at flotation of £1.6486 (giving £6.425m) compared to £1.16, the price shares were trading at on the day of exchange which gave a fair value of equity issued of £4.52m. This gave rise to the negative goodwill which was taken directly to the income statement. A further cash payment of £80,000 was made following the settlement of the completion accounts. Certain of the properties acquired have been disposed of since the year end.

In the one month following acquisition the subsidiary has contributed a profit before REIT conversion charge of £80,000 and a loss after REIT conversion charge of £210,000. If the acquisition had occurred on 1 October 2006, management estimate that the consolidated revenue for the Group would have been £950,000 higher and the consolidated profit before tax for the year would have been £460,000 higher.
In determining these amounts, management have assumed that the fair value adjustments that arose on the date of acquisition would have been the same if the acquisition had occurred on 1 October 2006.

Notes to the Financial Statements

for the year ended 30 September 2007

4 Net Rental Income

	2007 £000	2006 £000
Gross rental income	**13,101**	5,528
Property operating expenses	**(1,642)**	(420)
	11,459	5,108

Included within property operating expenses at 30 September 2007 is £219,899 (2006: £21,866) relating to impairments of trade receivables.

5 Administrative Expenses

a) The following fees have been paid to the Group's Auditors:

	2007 £000	2006 £000
Auditors' remuneration for audit services:		
Audit of parent company	**35**	3
Auditors' remuneration for non-audit services:		
Statutory audit of subsidiaries	**45**	30
Tax services	**43**	10
Other services supplied pursuant to such legislation	**190**	–
Services relating to corporate finance transactions	**28**	–

The other services supplied pursuant to such legislation relates to the services provided as reporting accountant during the flotation.

b) Included in administrative expenses are staff costs and directors' remuneration.

The average number of persons employed by the Group, including directors, was as follows:

	2007	2006
	Number of Employees	
Administration	**12**	4

The aggregate payroll costs of these people were as follows:

	2007 £000	2006 £000
Wages and salaries	**1,108**	504
Social security costs	**120**	62
Other pension costs	**22**	–
Equity settled share-based payments	**72**	–
	1,322	566

Directors' emoluments are disclosed separately in the Directors' Remuneration Report on pages 29 to 32.

5 Administrative Expenses continued

Share Award Schemes

The Company operates two share award schemes: a Company Share Option Plan for certain employees and a Long Term Incentive Plan for certain senior management. Both plans were adopted by the Company with effect from 2 May 2007.

On admission to the London Stock Exchange on 2 May 2007, the following number of shares were awarded. Details of the exercise price and the periods in which they may be exercised are given below.

Company Share Option Plan	Exercise Price p	Exercisable Between	**2007 Number 000**	2006 Number 000
2 May 2007	175.5	3 May 2010- 1 May 2017	**53**	–

	2007 £000	2006 £000
Fair value of options	**19**	–
Expense recognised in the year	**(3)**	–
Expense carried forward to be recognised in future years	**16**	–

The estimated fair value of the share options granted during the year have been calculated using the Black Scholes model. Inputs to the model are summarised below:

	2007	2006
Expected volatility	**23.46%**	–
Risk free interest rate	**5.12%**	–
Expected life of options	**5 years**	–
Expected dividend yield	**4.75%**	–
Weighted average share price	**£1.755**	–

The expected life of the options is based on historical data and the Company's expectations. It is not necessarily indicative of exercise patterns that may occur. The expected volatility reflects the assumptions that the historical volatility is indicative of future trends which may also not necessarily be the actual outcome. The volatility was calculated according to comparable data of companies with a similar activity.

Long Term Incentive Plan	Exercise Price p	Exercisable Between	**2007 Number 000**	2006 Number 000
2 May 2007	–	3 May 2010- 1 May 2017	**642**	–

	2007 £000	2006 £000
Fair value of award	**500**	–
Expense recognised in the year	**(69)**	–
Expense carried forward to be recognised in future years	**431**	–

Notes to the Financial Statements

for the year ended 30 September 2007

5 Administrative Expenses continued

The Monte Carlo model has been used to determine the fair value of the shares awarded under the Long Term Incentive Plan.

The assumptions used in the model were as follows:

	2007	2006
Expected volatility	27.3%	–
Risk free interest rate	5%	–
Expected life of options	3 years	–
Expected dividend yield	4.75%	–
Weighted average share price	£1.755	–

The scheme and its performance criteria are fully explained in the directors' remuneration report on pages 29 and 30.

The expected volatility rate used is the average of a selection of companies which have a similar profile to the Company, as the Company does not have sufficient trading history to use its own share price. The expected volatility is based on historical share prices of these companies over a period equal to the expected term of the awards. The companies used for these purposes are not members of the comparator group of companies for the total shareholder return performance condition.

No options or share awards were exercised as of the balance sheet date.

The fair value of the options and share awards were appraised by an independent appraisal company.

6 Net Other Income

	2007 £000	2006 £000
Other income	151	521
Other expenses	(126)	(44)
	25	477

Other income relates to insurance commission received and property management income from Castlemore Ventures Limited, see note 23. Other expenses relate to fees incurred on aborted property purchases.

7 Net Financing Costs

	2007 £000	2006 £000
Interest receivable	786	90
Fair value gains on derivative financial instruments (note 20)	516	1,040
Financial income	1,302	1,130
Bank loan interest	(7,606)	(3,850)
Other loan interest (note 23)	(2,466)	(2,022)
Head rents treated as finance leases	(108)	(49)
Financial expenses	(10,180)	(5,921)
Net financing costs	(8,878)	(4,791)

8 Taxation

	2007 £000	2006 £000
Current tax		
Corporation tax charged at 30% (2006: 30%)	**–**	–
REIT conversion charge	**4,584**	–
Adjustment to prior period	**–**	170
Total current tax	**4,584**	170
Deferred tax charge		
Origination and reversal of temporary differences	**(785)**	1,009
Total tax charge in the income statement	**3,799**	1,179

Reconciliation of Effective Tax Rate	2007 £000	2006 £000
(Loss)/profit before tax	**(4,262)**	4,717
Corporation tax in the UK of 30% (2006: 30%)	**(1,279)**	1,415
Tax relief available from REIT status	**1,279**	–
Effects of:		
REIT conversion charge	**4,584**	–
Non-deductible expenses	**–**	29
Underprovided in prior periods	**–**	170
Other differences	**–**	9
Indexation relief on investment properties	**–**	(444)
Release of deferred tax following REIT conversion	**(785)**	–
	3,799	1,179

From 11 May 2007, the Group has elected to join the UK REIT regime. As a result, the Group will be exempt from corporation tax on the profits and gains from its property investment business from this date, provided it continues to meet certain conditions. Non-qualifying profits and gains of the Group (the residual business) continue to be subject to corporation tax. The directors consider that all the rental income post 11 May 2007 originates from the Group's tax exempt business. Due to the availability of losses, no provision for corporation tax has been made in these accounts – either for the pre-REIT period, or the residual business in the post-REIT period.

On entering the UK REIT regime, a conversion charge equal to 2% of the gross market value of properties involved in the property rental business, at that date, became due.

9 Plant and Equipment

	Fixtures and Fittings £000	Computer Equipment £000	Total £000	2006 £000
Cost				
Additions	29	54	83	–
At 30 September 2007	29	54	83	–
Accumulated depreciation				
Charge for year	2	8	10	–
At 30 September 2007	2	8	10	–
Net book value				
At 30 September 2007	**27**	**46**	**73**	**–**
At 30 September 2006	–	–	–	–

Notes to the Financial Statements

for the year ended 30 September 2007

10 Investment Properties

	Leasehold Investment Properties £000	Freehold Investment Properties £000	Total £000
At 1 October 2005	5,284	14,842	20,126
Additions	20,117	98,094	118,211
Disposals	–	(1,852)	(1,852)
Fair value adjustments	1,606	3,448	5,054
At 30 September 2006	27,007	114,532	141,539
Additions	18,378	98,252	116,630
Disposals	–	(1,056)	(1,056)
Fair value adjustments	(3,797)	(2,627)	(6,424)
Investment properties held for sale	–	(3,081)	(3,081)
At 30 September 2007	**41,588**	**206,020**	**247,608**

Investment properties held for sale at the balance sheet date are shown separately as current assets as required by IFRS 5. These assets no longer meet the investment criteria of the Group and subsequent to the year end have been sold at auction.

The investment properties have all been revalued to their fair value at 30 September 2007.

All properties acquired since 28 March 2007, together with a sample selected by the valuers of 25% of the portfolio have been valued by Allsops, a firm of independent chartered surveyors. The valuations were undertaken in accordance with the Royal Institute of Chartered Surveyors Appraisal and Valuation Standards on the basis of market value. Market value is defined as the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's length transaction, after proper marketing wherein the parties had each acted knowledgably, prudently and without compulsion.

The remainder of the portfolio has been valued by the directors who have an appropriate recognised professional qualification and recent experience in the location and category of property being valued.

All rental income recognised in the income statement is generated by the investment properties held and all direct operating expenses incurred resulted from investment properties that generated rental income.

A reconciliation of the portfolio valuation at 30 September 2007 to the total value given in the consolidated balance sheet for investment properties is as follows:

	2007 £000	2006 £000
Portfolio valuation	**249,296**	140,196
Items not revalued	**40**	725
Investment properties held for sale	**(3,081)**	–
Head leases treated as finance leases under IAS 17	**1,353**	618
Total per consolidated balance sheet	**247,608**	141,539

11 Investment in Joint Ventures

The Group held an investment in a joint venture at 30 September 2006 which represented 75% of the issued ordinary share capital. On admission to the London Stock Exchange on 2 May 2007, the Company disposed of its investment in Castle Marinas Limited for an amount equal to its carrying value. The company was incorporated in the United Kingdom (and its 100% owned subsidiaries: Owlpower Limited and Buckden Marina Limited), whose principal activities were the operation of marinas.

The investment was treated as a joint venture, despite the majority shareholding, due to the existence of a contractual agreement (being the shareholder agreement) which distinguished interests that involve joint control between all venturers.

The summarised financial information in respect of the Group's share of the joint venture is shown, for information purposes only, below.

In accordance with IAS 28, the Group's share of losses was restricted to nil because there was no legal or constructive obligation for the Group to make payments to settle the joint venture liabilities. The Group's share of the cumulative unrecognised losses of the joint venture are shown below.

	2006 £000
Non-current assets	3,665
Current assets	274
Non-current liabilities	(1,214)
Current liabilities	(2,847)
Net liabilities	(122)
Income	279
Expenses	(401)
Unrecognised loss for the period	(122)

12 Deferred Tax Assets and Liabilities

Recognised Deferred Tax Assets and Liabilities

Deferred tax assets and liabilities are attributable to the following items:

	Assets		Liabilities		Net	
	2007 £000	2006 £000	**2007 £000**	2006 £000	**2007 £000**	2006 £000
Investment property	**–**	595	**–**	(1,434)	**–**	(839)
Other items	**–**	21	**–**	(342)	**–**	(321)
Tax value of loss carry-forwards recognised	**–**	375	**–**	–	**–**	375
Net tax assets/(liabilities)	**–**	991	**–**	(1,776)	**–**	(785)

There are no unrecognised deferred tax assets at 30 September 2007 (2006: £Nil).

Deferred tax accrued at the conversion date in respect of assets and liabilities on unrealised losses and gains on revaluation of the Group's investment properties has been released to the income statement. This is on the basis that these temporary differences will no longer affect the future UK tax position of the Group, on account of the Group's conversion to REIT status. The same analysis has been applied to the deferred tax liability previously provided on financial instruments. The previous deferred tax asset recognised in respect of tax losses brought forward has also been released to the income statement. Due to the Group's conversion to REIT status, it is no longer considered probable that taxable profits will be available in the future against which these losses can be utilised.

Notes to the Financial Statements

for the year ended 30 September 2007

13 Trade and Other Receivables

	2007 £000	2006 £000
Amounts due from jointly controlled entities	–	973
Trade receivables	**4,092**	1,064
Other receivables	**568**	1,446
Prepayments	**169**	80
	4,829	3,563

14 Cash

	2007 £000	2006 £000
Bank balances	**5,735**	2,891
Bank overdrafts	**(115)**	(91)
Cash in the statement of cash flows	**5,620**	2,800

15 Interest-Bearing Loans and Borrowings

	2007 £000	2006 £000
Non-current liabilities		
Secured bank loans	**98,149**	106,230
Other loans	–	30,353
	98,149	136,583
Current liabilities		
Current portion of secured bank loans	–	3,231

All bank borrowings are secured by fixed charges over certain of the Group's property assets and floating charges over the companies which own the assets charged.

For more information about the Group's exposure to interest rate risk, see note 20.

16 Trade and Other Payables

	2007 £000	2006 £000
Trade payables	**808**	438
Other taxation and social security	**5,103**	96
Other payables	**2,200**	758
Accruals and deferred income	**3,412**	3,095
	11,523	4,387

17 Leasing

Obligations Under Finance Leases

Finance lease liabilities on head rents are payable as follows:

	Principal £000	Interest £000	Minimum Lease Payment £000
At 1 October 2006	5,550	(4,932)	618
Additions	6,233	(5,498)	735
At 30 September 2007	**11,783**	**(10,430)**	**1,353**

All leases expire in more than five years.

18 Capital and Reserves

Reconciliation of Movement in Capital and Reserves

	Share Capital £000	Share Premium £000	Reserves £000	Retained Earnings £000	Total £000
At 1 October 2005	800	–	31	(1,000)	(169)
Total recognised income and expense	–	–	–	3,538	3,538
At 30 September 2006	800	–	31	2,538	3,369
Issue of shares	19,298	137,331	3,742	–	160,371
Own shares acquired	–	–	–	(3,978)	(3,978)
Cancellation of share premium	–	(137,331)	–	137,331	–
Share-based payments	–	–	–	72	72
Total recognised income and expense	–	–	–	(8,061)	(8,061)
At 30 September 2007	**20,098**	**–**	**3,773**	**127,902**	**151,773**

Share Capital

	2007 Ordinary 20p Shares		2006 Ordinary £1 Shares	
	Number 000	Amount £000	Number 000	Amount £000
Allotted, called up and fully paid	**100,493**	**20,098**	800	800

The shares in issue at 30 September 2006 were divided into 600,000 'A' Ordinary £1 Shares; 100,000 'B' Ordinary £1 Shares and 100,000 'C' Ordinary £1 Shares.

Prior to the flotation of the Company the share capital was reorganised by way of subdivision and reclassification of its Ordinary Shares. The "A", "B" and "C" £1 Ordinary Shares were sub-divided into 20p shares, giving each shareholder five shares for each individual share held, and each share reclassified as an Ordinary Share.

Following this the authorised share capital was increased to £150,000,000 via the creation of 746,000,000 new Ordinary Shares.

On 2 May 2007, the Company issued 91,954,023 Ordinary Shares at £1.74 per share in an initial public offering (IPO) and all of its Ordinary Shares were admitted to the Official List of the London Stock Exchange. The proceeds received from the IPO amounted to £160,000,000, net of issuance costs of £4,278,425. On the same day the Employee Benefit Trust subscribed for 641,521 shares at their nominal value. In addition on 29 August 2007 the Company issued a further 3,897,246 shares in order to purchase Gilfin Property Holdings Limited.

At 30 September 2007 the Company held 2,953,750 shares in Treasury (2006: Nil).

Notes to the Financial Statements

for the year ended 30 September 2007

18 Capital and Reserves continued

Share Premium

The share premium arose following the issue and subscription for shares with a nominal value of 20p at £1.74 on 2 May 2007. Subsequently the Company applied to the courts to have the share premium reserve converted to a distributable reserve.

Reserves

The value of shares issued to purchase Gilfin Property Holdings Limited in excess of their nominal value has been shown as a separate reserve in accordance with the Companies Act 1985.

Calculation of Net Asset Value Per Share (NAV)

	2007 £000	2006 £000
Net assets	**151,773**	3,369
Mark to market adjustment of fixed rate loan (see note 20)	**2,962**	–
Adjusted net assets	**154,735**	3,369

	2007 Number 000	2006 Number 000
Allotted, called up and fully paid shares	**100,493**	800
Treasury shares	**(2,954)**	–
Number of shares	**97,539**	800

NAV per share	**156p**	421p
Adjusted NAV per share	**159p**	421p

19 Earnings Per Share

Basic Earnings Per Share

The calculation of basic earnings per share was based on the (loss)/profit attributable to ordinary shareholders and a weighted average number of Ordinary Shares outstanding, calculated as follows:

(Loss)/profit Attributable to Ordinary Shares

	2007 £000	2006 £000
(Loss)/profit for the year	**(8,061)**	3,538

Weighted Average Number of Ordinary Shares

	2007 Number 000	2006 Number 000
Issued Ordinary Shares at 1 October 2006	**800**	800
Effect of subdivision of shares	**1,324**	1,324
Effect of own shares held	**(134)**	–
Effect of shares issued	**38,383**	–
Weighted average number of Ordinary Shares at 30 September 2007	**40,373**	2,124

The comparative weighted average number of shares has been adjusted for the effect of the subdivision of shares which took place in the current year in accordance with IAS 33.

Diluted Earnings Per Share

There is no difference between basic and diluted earnings per share as the effect of share options in the year is anti-dilutive.

20 Financial Instruments and Risk Management

The Group is subject to the following financial risks: credit risk, liquidity risk and interest rate risks.

Credit risk – the Group's principal financial assets are cash, bank balances, trade and other receivables. The Group's credit risk is mainly attributable to its trade receivable balances. The amounts carried in the balance sheet are net of provisions for impairments. Provisions are made where there is evidence that the Group will not be able to collect the amounts due. The Group has no significant concentration of credit risk due to the large number of small balances owed by a wide range of tenants.

Liquidity risk – the Group maintains a combination of long-term and short-term committed facilities that are designed to ensure that it has sufficient available funds for ongoing operations and to meet planned future investments.

Interest rate risk – the Group does not speculate in treasury products. It uses these products to minimise the exposure to interest rate fluctuations. The Group borrows from UK banks at fixed and floating rates of interest based on LIBOR and uses hedging mechanisms to achieve an interest rate profile where the majority or borrowings are fixed or capped. The Group's policy is to hedge between 60% and 100% of its interest rate exposure. At 30 September 2007, 100% (2006: 97%) of the Group's net debt was fixed or protected, with a further £50,378,000 of swaps in place to cover future debt as it is drawn down.

Financial Instruments

Derivative financial instruments are shown in the consolidated balance sheet as follows:

	At 1 October 2006 £000	**Mark to Market £000**	**At 30 September 2007 £000**
Non-current assets	772	**262**	**1,034**
Current assets	369	**184**	**553**
Non-current liabilities	(70)	**70**	**–**
Net value	1,071		**1,587**
Amount credited to income statement		**516**	

Notes to the Financial Statements

for the year ended 30 September 2007

20 Financial Instruments and Risk Management continued

The Group's interest rate swaps in place at 30 September 2007, did not qualify as effective swaps for hedge accounting under the criteria set out in IAS 39.

A summary of the swaps and their maturity dates are as follows:

Maturity Date	Amount £000	Rate %	Fair Value 2007 £000	Fair Value 2006 £000	Movements in Income Statement £000
30 April 2013	54,000	5.06 – 5.62	**582**	(53)	**635**
31 January 2017	26,378	4.8500	**1,005**	–	**1,005**
	80,378		**1,587**	(53)	**1,640**
Swaps in place at 30 September 2006					
25 April 2010	77,000	4.5050 – 5.2300	**–**	905	**(905)**
18 April 2016	14,431	4.7225	**–**	219	**(219)**
	171,809		**1,587**	1,071	**516**

The financial derivatives included in the above tables were valued by JC Rathbone Associates Limited, financial risk consultants, using a discounted cash flow model and published market information.

The Group does not trade financial derivatives.

Fair Value

The fair value of the Group's financial assets is not considered to be materially different from the book value.

The fair value of the Group's financial liabilities is not considered to be materially different from the book value with the exception of the following fixed rate loan held with Barclays Capital.

	2007 £000	2006 £000
Fixed rate loan		
Carrying value of loan	**68,775**	–
Mark to market adjustment	**(2,962)**	–
Fair value of loan	**65,813**	–

20 Financial Instruments and Risk Management continued

Effective Interest Rates and Re-Pricing Analysis

In respect of income-earning financial assets and interest-bearing financial liabilities, the following table indicates their effective interest rates at the balance sheet date and the periods in which they mature or, if earlier, are re-priced. The floating interest rates are tied to LIBOR.

30 September 2007

	Effective Interest Rate %	Total £000	0 to 1 Year £000	1 to < 2 Years £000	2 to < 3 Years £000	3 to < 4 Years £000	4 to < 5 Years £000	5 Years and Over £000
Cash and cash equivalents	Floating	5,734	5,734	–	–	–	–	–
Bank overdrafts	Floating	(115)	(115)	–	–	–	–	–
Secured bank loans	5.595%	(68,775)	–	–	–	–	–	(68,775)
Secured bank loans	Floating	(29,374)	–	–	–	–	–	(29,374)
Total		**(92,530)**	**5,619**	**–**	**–**	**–**	**–**	**(98,149)**

In respect of income earning financial assets and interest bearing financial liabilities, the following table indicates their effective interest rates at the balance sheet date and the periods in which they mature or, if earlier, are re-priced.

30 September 2006

	Effective Interest Rate %	Total £000	0 to 1 Year £000	1 to < 2 Years £000	2 to < 3 Years £000	3 to < 4 Years £000	4 to < 5 Years £000	5 Years and Over £000
Cash and cash equivalents	Floating	2,891	2,891	–	–	–	–	–
Bank overdrafts	Floating	(91)	(91)	–	–	–	–	–
Secured bank loans	Floating	(109,461)	(3,231)	(1,529)	(1,503)	(1,477)	(1,452)	(100,269)
Other loans	11.7%	(30,353)	–	–	–	–	–	(30,353)
Total		**(137,014)**	**(431)**	**(1,529)**	**(1,503)**	**(1,477)**	**(1,452)**	**(130,622)**

21 Operating Lease Arrangements

a) As lessee

Future minimum lease payments payable by the Group under non-cancellable operating leases were as follows:

	Plant and Equipment 2007 £000	Plant and Equipment 2006 £000
Operating leases which expire:		
Two to five years	**54**	–

b) As lessor

Future minimum lease payments receivable by the Group under non-cancellable operating leases were as follows:

	2007 £000	2006 £000
Operating leases which expire:		
Within one year	**1,237**	1,886
One to two years	**1,711**	1,385
Two to five years	**2,890**	3,638
Over five years	**11,425**	6,885
	17,263	13,794

Notes to the Financial Statements

for the year ended 30 September 2007

22 Capital Commitments

At 30 September 2007 the Group had contracted capital expenditure for which no provision has been made in these financial statements of £272,000 (2006: £7,252,000).

23 Related Parties

Identity of Related Parties

The Group has related party relationships with its subsidiaries (see note 24), jointly controlled entity (see note 11) and with its key management personnel.

Transaction with Key Management Personnel

The only transactions with key management personnel relate to remuneration which is set out in the Directors' Remuneration Report on pages 29 to 32.

The key management personnel of the Group for the purposes of related party disclosures under IAS 24 comprise all executive and non-executive directors.

During the year the Group received income from various associated undertakings for property management services provided as follows:

	2007 £000	2006 £000
Castlemore Securities Limited	**–**	2
Castlemore Rangers (3) Limited	**–**	2
Castlemore Ventures Limited	**18**	38
	18	42

These companies are all 100% subsidiaries of Castlemore Holdings Limited, a 75% shareholder until 2 May 2007.

At the year end the following balances were owed by/(to) the following associated companies and jointly controlled entity by the Company:

	2007		2006	
	Due in Less Than One Year £000	**Due in More Than One Year £000**	Due in Less Than One Year £000	Due in More Than One Year £000
Castle Marinas Limited	**–**	**–**	973	–
Castlemore Holdings Limited	**–**	**–**	–	(30,353)
Castlemore Securities Limited	**(164)**	**–**	(437)	–
Castlemore Ventures Limited	**54**	**–**	36	–

There are no set repayment dates for these balances.

23 Related Parties continued

Interest was charged by Castlemore Holdings Limited at a rate of 8% and 12.5%. The charge to 30 September 2007 was £2,466,000 (2006: £2,022,000).

Interest was charged by the Company to Castle Marinas Limited at a rate of 17.5%, interest received to 30 September 2007 was £282,000 (2006: £52,000).

In addition income was received from Castlemore Securities Limited of £66,000 in respect of commission it received on insurance premiums incurred in insuring the property portfolio. Following flotation the Group now insures its own properties.

At the time of the flotation a transitional services agreement was entered into with Castlemore Securities Limited ("CSL") whereby CSL would continue to provide certain management services on a transitional basis to the Group. The charge for the year in respect of these services was £2,680 (2006: £Nil).

24 Group Entities

Control of the Group

There is no ultimate controlling party.

Subsidiaries

	Country of Incorporation	Ownership Interest*	
		2007	2006
NOS Limited	United Kingdom	**100%**	100%
NOS 2 Limited	United Kingdom	**100%**	100%
NOS 3 Limited	United Kingdom	**100%**	100%
NOS 4 Limited	United Kingdom	**100%**	100%
NOS 5 Limited	United Kingdom	**100%**	100%
NOS 6 Limited	United Kingdom	**100%**	–
NOS 7 Limited	United Kingdom	**100%**	–
NOS 8 Limited	United Kingdom	**100%**	–
Gilfin Property Holdings Limited	United Kingdom	**100%**	–

* All interests are in Ordinary Shares.

Company Balance Sheet

as at 30 September 2007

	Note	2007 £000	2006 £000
Fixed assets			
Plant and equipment	C2	**73**	–
Investments	C3	**147,455**	–
Current assets			
Debtors	C4	**11,063**	31,809
Cash		**–**	183
		158,591	31,992
Creditors: Amounts falling due within one year	C5	**(2,115)**	(495)
Net current assets		**156,476**	31,497
Total assets less current liabilities		**–**	31,497
Creditors: Amounts falling due after one year	C6	**–**	(30,353)
Net assets		**156,476**	1,144
Capital and reserves			
Share capital	C7	**20,098**	800
Reserves	C8	**3,742**	–
Profit and loss account	C8	**132,636**	344
Shareholders' funds		**156,476**	1,144

These financial statements were approved by the Board of directors on 11 January 2008 and were signed on its behalf by:

M E Riley
Joint CEO

N J Gregory
Joint CEO

Notes to the Company Financial Statements

for the year ended 30 September 2007

C1 Accounting Policies

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

On 16 March 2007, the Company changed its name from Castlemore Capital Limited to The Local Shopping REIT plc and re-registered as a public company, formerly it was registered as a private company.

Basis of Preparation

The financial statements have been prepared in accordance with applicable UK Accounting Standards and under the historical cost accounting rules.

In preparing the financial statements for the current year the Company has adopted the following new Financial Reporting Standards (FRS):

- FRS 20 – Share-Based Payments

Cash Flow Statement

Under FRS 1, the Company is exempt from the requirement to prepare a cash flow statement on the grounds that the Company is included in its own published consolidated financial statements.

Related Party Transactions

The Company has taken advantage of the exemption in FRS 8 – Related Party Transactions and has not disclosed transactions or balances with entities which form part of the Group as these consolidated financial statements include the results of these entities.

Investments

Investments in subsidiary undertakings are stated at cost less provisions due to a diminution in the net realisable value.

Plant and Equipment

All plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure which is directly attributable to the acquisition of the asset.

Depreciation is charged to the profit and loss account on the following basis:

- Fixtures and fittings – 15% reducing balance; and
- Computer equipment – straight line basis over three years.

Taxation

The charge for taxation is based on the result for the period 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.

Share-Based Payments

The Company operates equity settled, share-based compensation plans comprising awards under a Long Term Incentive Plan ("LTIP") and a Company Share Option Plan ("CSOP") for certain employees. The fair values of these schemes are measured at their fair value at the date of grant. The fair value is then recognised as an employee cost, with a corresponding increase in equity, on a straight line basis over the vesting period, based on the Group's estimate of the shares that will eventually vest.

The fair value of each scheme is measured using an option pricing model. The awards under the LTIP scheme are measured using a Monte Carlo simulation model and the awards under the CSOP scheme are measured using a Black Scholes model.

Notes to the Company Financial Statements

for the year ended 30 September 2007

C1 Accounting Policies continued

Ordinary Share Capital

External costs directly attributable to the issue of new shares are shown in equity as a deduction from the proceeds.

Shares which have been repurchased are classified as Treasury shares and shown in retained earnings. They are recognised at the trade date for the amount of consideration paid, together with directly attributable costs. This is presented as a deduction from total equity.

Profit for the Financial Year

The Company has taken advantage of Section 230 of the Companies Act 1985 and has not included its own profit and loss account in these financial statements. The Company's loss for the year was £1,133,000 (2006: £326,000 profit).

C2 Plant and Equipment

	Fixtures and Fittings £000	Computer Equipment £000	Total £000
Cost			
Additions	29	54	83
At 30 September 2007	29	54	83
Accumulated depreciation			
Charge for year	2	8	10
At 30 September 2007	2	8	10
Net book value			
At 30 September 2007	**27**	**46**	**73**
At 30 September 2006	–	–	–

C3 Fixed Asset Investments

	Investment in Joint Venture £000	Shares in Group Undertakings £000	Total £000
Cost			
At 1 October 2006	–	–	–
Additions	–	147,455	147,455
Disposals	–	–	–
At 30 September 2007	–	147,455	147,455
Provisions			
At 1 October 2006 and 30 September 2007	–	–	–
Net book value			
At 30 September 2007	**–**	**147,455**	**147,455**
At 30 September 2006	–	–	–

During the year the Company acquired the entire share capital of Gilfin Property Holdings Limited for a combination of cash and the issue of new equity. The Company holds a portfolio of properties located in Scotland and London.

C3 Fixed Asset Investments continued

The consideration paid was as follows:

	£000
Cash paid including costs of acquisition*	6,835
Fair value of new equity issued	4,520
	11,355

* including costs associated with the acquisition of £330,000.

The consideration agreed for the Company was £12.85m comprising £6.425m of cash (which increased by £80,000 following the settlement of the completion accounts) and £6.425m of equity. The equity element was calculated based on 3,897,246 shares with a value of £1.6486. However, on the day of exchange the shares were trading at £1.16 giving a fair value of the equity consideration of £4.52m. This resulted in a total cost of investment of £11.355m, including costs of acquisition of £330,000.

During the year the following loan balances owed by subsidiaries were exchanged for Ordinary Shares.

	£000
NOS 2 Limited	40,000
NOS 3 Limited	5,600
NOS 4 Limited	68,500
NOS 5 Limited	22,000
	136,100

During the year the Company disposed of its joint venture investment for an amount equal to its carrying value, which was a 75% holding in Castle Marinas Limited, a company incorporated in Great Britain whose principal activity is the operation of marinas.

The companies in which the Company's interests at the year end are more than 20% are as follows:

Subsidiary Undertaking	Nature of Business	Ownership Interest*
NOS Limited	Property trading	100%
NOS 2 Limited	Property investment	100%
NOS 3 Limited	Property investment	100%
NOS 4 Limited	Property investment	100%
NOS 5 Limited	Property investment	100%
NOS 6 Limited	Property investment	100%
NOS 7 Limited	Property investment	100%
NOS 8 Limited	Property investment	100%
Gilfin Property Holdings Limited	Property investment	100%

* All interests are in Ordinary Shares.

All of the above companies are incorporated in Great Britain.

C4 Debtors

	2007 £000	2006 £000
Amounts owed by Group undertakings	**11,006**	30,783
Amounts owed by associated undertakings	**–**	1,008
Other debtors	**27**	18
Prepayments	**30**	
	11,063	31,809

Notes to the Company Financial Statements

for the year ended 30 September 2007

C5 Creditors: Amounts Falling Due Within One Year

	2007 £000	2006 £000
Bank overdrafts	**115**	19
Trade creditors	**229**	6
Amounts owed to associated undertakings	**–**	436
Other taxation and social security	**49**	23
Other creditors	**1,347**	4
Accruals	**375**	7
	2,115	495

C6 Creditors: Amounts Falling Due After One Year

	2007 £000	2006 £000
Amounts owed to associated undertakings	**–**	30,353

C7 Called Up Share Capital

	2007 Ordinary 20p Shares		2006 Ordinary £1 Shares	
	Number 000	Amount £000	Number 000	Amount £000
Authorised	**746,000**	**150,000**	800	800
Allotted, called up and fully paid	**100,493**	**20,098**	800	800

	Share Capital £000
At 1 October 2006	800
Issue of shares	19,298
At 30 September 2007	**20,098**

The shares in issue at 30 September 2006 were divided into 600,000 ‘A’ Ordinary £1 Shares; 100,000 ‘B’ Ordinary £1 Shares and 100,000 ‘C’ Ordinary £1 Shares.

Prior to the flotation of the Company the share capital was reorganised by way of subdivision and reclassification of its Ordinary Shares. The “A”, “B” and “C” £1 Ordinary Shares were sub-divided into 20p shares, giving each shareholder five shares for each individual share held, and each share reclassified as an Ordinary Share.

Following this the authorised share capital was increased to £150,000,000 via the creation of 746,000,000 new Ordinary Shares.

On 2 May 2007, the Company issued 91,954,023 Ordinary Shares at £1.74 per share in an Initial Public Offering (“IPO”) and all of its Ordinary Shares were admitted to the Official List of the London Stock Exchange. The proceeds received from the IPO amounted to £160,000,000, net of issuance costs of £4,278,425. On the same day the Employee Benefit Trust subscribed for 641,521 shares at their nominal value. In addition on 29 August 2007 the Company issued a further 3,897,246 shares in order to purchase Gilfin Property Holdings Limited.

At 30 September 2007 the Company held 2,953,750 shares in Treasury (2006: Nil).

C8 Reserves

	Share Premium £000	Reserves £000	Profit and Loss Account £000	Total £000
At 1 October 2006	–	–	344	344
Issue of shares	137,331	3,742	–	141,073
Own shares acquired	–	–	(3,978)	(3,978)
Cancellation of share premium	(137,331)	–	137,331	–
Share-based payments	–	–	72	72
Retained loss for the year	–	–	(1,133)	(1,133)
At 30 September 2007	**–**	**3,742**	**132,636**	**136,378**

Share Premium

The share premium arose following the issue and subscription for shares with a nominal value of 20p at £1.74 on 2 May 2007. Subsequently the Company applied to the courts to have the share premium reserve converted to a distributable reserve.

Reserves

The value of shares issued to purchase Gilfin Property Holdings Limited in excess of their nominal value has been shown as a separate reserve in accordance with the Companies Act 1985.

C9 Related Party Transactions

During the year the Company received income from various associated undertakings for property management services provided as follows:

	2007 £000	2006 £000
Castlemore Securities Limited	**–**	2
Castlemore Ranger (3) Limited	**–**	2
Castlemore Ventures Limited	**18**	38
	18	42

These companies are all 100% subsidiaries of Castlemore Holdings Limited, a 75% shareholder until 2 May 2007.

Interest was charged by Castlemore Holdings Limited at a rate of 12.5% and 8%. The charge to 30 September 2007 was £2,466,000 (2006: £2,022,000).

Interest was charged by the Company to Castle Marinas Limited at a rate of 17.5%, interest received to 30 September 2007 was £282,000 (2006: £52,000).

At the time of flotation a transitional services agreement was entered into with Castlemore Securities Limited ("CSL") whereby CSL would continue to provide certain management services on a transitional basis to the Group. The charge for the year in respect of these services was £2,680 (2006: £Nil).

C10 Ultimate Controlling Party

There is no ultimate controlling party.

Glossary of Terms

Adjusted net asset value ("Adjusted NAV") per share
Adjusted NAV is calculated as shareholders' funds, plus the mark to market adjustment of the fixed rate loan, divided by the number of shares in issue at the year end, excluding Treasury shares.

Earnings per share ("EPS")
EPS is calculated as profit attributable to shareholders divided by the weighted average number of shares in issue in the year.

Equivalent yield
Equivalent yield is a weighted average of the initial yield and reversionary yield and represents the return a property will produce based upon the timing of the income received. In accordance with usual practice, the equivalent yields (as determined by the Group's external valuers) assume rent received annually in arrears and on gross values including prospective purchasers' costs (including stamp duty, agents and legal fees.

Funds from operations ("FFO")
FFO is a term adopted by the National Association of Real Estate Investment Trusts. It is calculated as net income adjusted for depreciation of investment properties and gains/losses on sales of investment properties.

Head lease
A head lease is a lease under which the Group holds an investment property.

Initial yield
Initial yield is the annualised net rent generated by a property expressed as a percentage of the property valuation. In accordance with usual practice the property value is grossed up to include prospective purchasers' costs.

Interest cover
Interest cover is the number of times financial expenses less the head rents treated as finance leases adjustment, is covered by underlying profit before net financing costs, taxation, revaluation adjustments and other income.

Interest rate swap
An interest rate swap is a financial instrument where two parties agree to exchange an interest rate obligation for a predetermined amount of time. These are used by the Group to convert floating rate debt to fixed rates.

Investment Property Databank Ltd ("IPD")
IPD produces an independent benchmark of property returns.

Initial Public Offering ("IPO")
An IPO is the first sale of shares by a privately owned company on a Stock Exchange. LSR issued its shares for sale on 2 May 2007.

London Interbank Offered Rate ("LIBOR")
LIBOR is the interest rate charged by one bank to another bank for lending money.

Loan to value ("LTV")
Loan to value is the ratio of debt, excluding any mark-to-market adjustments, to the value of investment properties.

Market value
Market value is the estimated amount for which a property should exchange on the date of valuation between a willing buyer and willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

Market rent
Market rent is the estimated amount for which a property should lease on the date of valuation between a willing lessor and a willing lessee on appropriate lease terms, in an arm's length transaction, after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

Mark-to-market adjustment
Mark-to-market adjustment is an accounting adjustment to change the book value of an asset or liability to its market value.

Net asset value ("NAV") per share
NAV per share is calculated as shareholders' funds divided by the number of shares in issue at the year end excluding Treasury shares.

Real Estate Investment Trust ("REIT")
A REIT is a listed property company which qualifies for and has elected into a tax regime, which exempts qualifying UK property rental income and gains on investment property disposals from corporation tax. LSR converted to REIT status on 11 May 2007.

Reversionary yield
Reversionary yield is the annualised net rent that would be generated by a property if it were fully let at market rent expressed as a percentage of the property valuation. In accordance with usual practice the property value is grossed up to include prospective purchasers' costs.

Shareholder Information

Registered Office
The Local Shopping REIT plc
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Key dates and other important information are available on our website: www.localshoppingreit.co.uk

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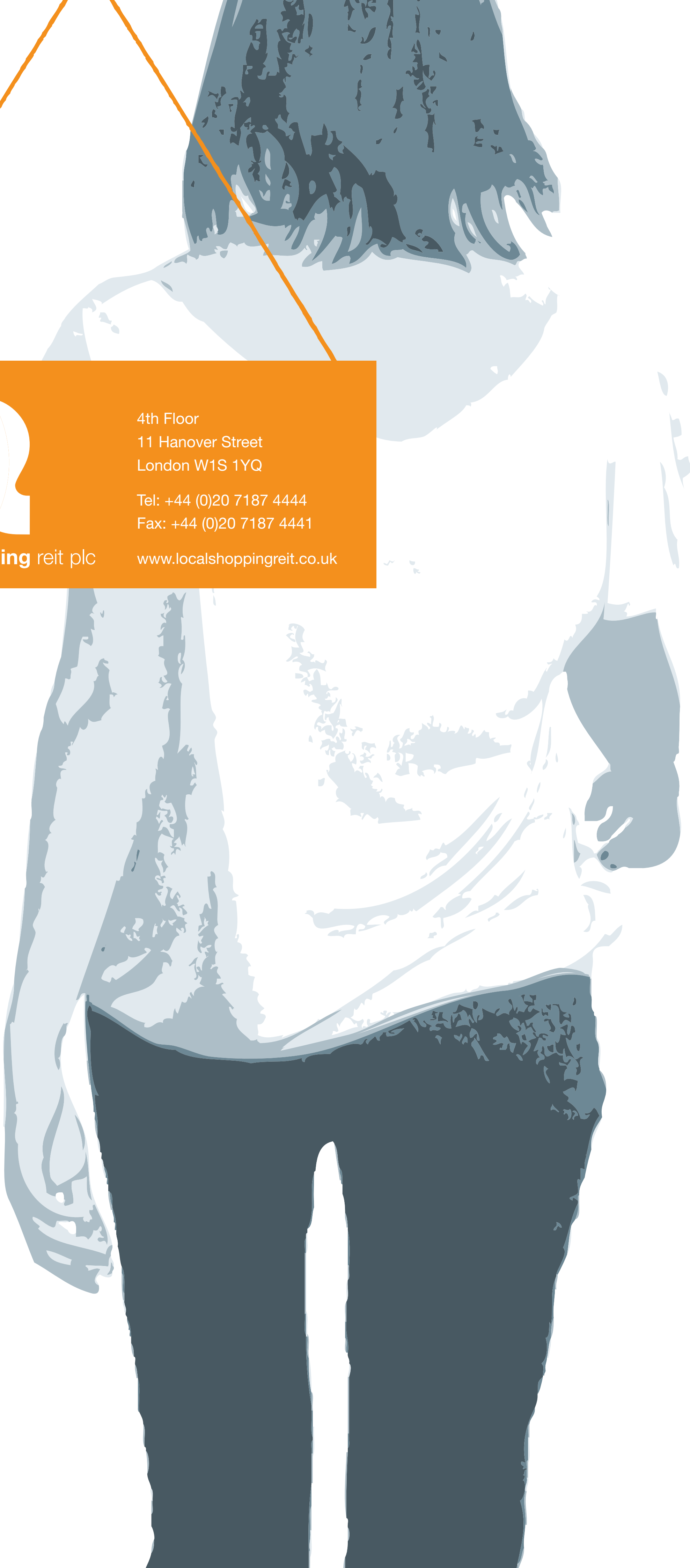

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