

Appendix I

Additional commentary on LST contracts



Norwich Union, DVLA, Barclays, Telereal II, Leicester Grammar School

| | Property | Finance Lease Debtor at March 2007 | Total capital commitment as finance lease | Return on Finance Lease | Other PBT 2006/07 ⁽¹⁾ | Contract Expiry |
|--------------------------|----------------------------|------------------------------------|---|-------------------------|----------------------------------|--|
| Norwich Union | £43.1m operating property | £73.2m | £94m | 8% | £2.2m ⁽²⁾ | 2029 |
| DVLA | 0 | £24.1m | £68m | 9% | £0.7m | 2025 |
| Barclays | £27.9m investment property | - | - | - | £0.7m | Ongoing – reducing profits as liabilities extinguished |
| Telereal II | - | - | - | - | £16.1m | March 2010 |
| Leicester Grammar School | - | - | £30.5m | 5.85% + RPI | - | 2043 |

(1) Excluding finance lease interest income and rents from operating and investment properties

(2) Excluding £1.2m profit on disposal of property in Perth

Strong track record of execution on existing contracts

ADDITIONAL VALUE IN THESE CONTRACTS COMES FROM:

ANY EXCESS VALUE ABOVE BOOK COST FOR OPERATING PROPERTIES WHICH WAS HIGHLIGHTED BY THE DECEMBER 2006 VALUATION FOR REIT CONVERSION PURPOSES

ANY EXCESS VALUE IN THE FINANCE LEASES ATTRIBUTABLE TO THE DISCOUNT RATES USED FOR THE FINANCE LEASES BEING TOO HIGH FOR AN INCOME STREAM FROM THESE COUNTER PARTIES ONCE THE RISK ON THE DEVELOPMENT AND REFURBISHMENT PROJECTS HAS BEEN CLOSED OUT.

ADDITIONAL SOURCES OF PROFIT NOT DIRECTLY ATTRIBUTABLE TO PROPERTY OWNERSHIP OR FINANCE LEASES (AS IN THE PENULTIMATE COLUMN OF THE SLIDE).

THE NORWICH UNION CONTRACT HAD £117M IN THE BALANCE SHEET AT 31 MARCH 2007. THIS WAS MADE UP, FIRSTLY, OF £43M FOR OPERATING PROPERTIES WHICH WERE RE-VALUED AT 31 DECEMBER 2006 BY KNIGHT FRANK FOR REIT CONVERSION PURPOSES AT £52M (I.E., AN EXCESS OF £9M ABOVE CURRENT BOOK VALUE). SECONDLY, THERE WAS A FINANCE LEASE OF £73M. THE FINANCE LEASE RELATES TO REFURBISHMENT WORKS WHICH, WHEN COMPLETED IN DECEMBER 2007, WILL RISE TO £94M. THE FINANCE LEASE IS PRICED AT A DISCOUNT RATE OF 8%. OTHER INCOME FROM THE CONTRACT RELATES TO MAINTENANCE AND LCCE SERVICES AND PROVIDES A NET CONTRIBUTION TO PBT FOR THE YEAR TO MARCH 2007 OF £2.2M. THE CONTRACT RUNS TO 2029.

UNDER THE ORIGINAL CONTRACT WITH DVLA, OUR REMIT WAS TO REFURBISH THE DVLA HEADQUARTERS IN SWANSEA FOR SOME £25M AND TO MANAGE THEIR SHORT LEASEHOLD REGIONAL AND LOCAL OFFICE NETWORK ACROSS THE COUNTRY. THE FINANCE LEASE INTEREST IS PRICED ON THE BASIS OF A DISCOUNT RATE OF 9%. WE HAVE SINCE BEEN AWARDED 3 CONTRACT EXTENSIONS FOR FURTHER DEVELOPMENT AND REFURBISHMENT WORK IN SWANSEA WHICH WILL AGAIN BE TREATED AS FINANCE LEASES AND WILL, UPON COMPLETION, BE HELD IN THE BALANCE SHEET AT £43M WITH PRICING ON A CONSISTENT BASIS. WE ARE IN DISCUSSIONS ABOUT A FURTHER POTENTIAL DEVELOPMENT OF AROUND £10M. OUR PBT CONTRIBUTION FROM MANAGING THE LOCAL AND REGIONAL OFFICE NETWORK IS APPROXIMATELY £0.7M P.A.

FOR BARCLAYS BANK, WE ACQUIRED AN INVESTMENT PROPERTY IN COVENTRY WHICH IS VALUED AT 6 MONTHLY INTERVALS BY KNIGHT FRANK, AND WAS VALUED AT MARCH 2007 AT £27.9M. WE ALSO UNDERTOOK TO MANAGE THE DISPOSAL OF A SURPLUS LEASEHOLD ESTATE OF 285,000 SQ FT WHICH WAS ORIGINALLY 60% VACANT AND WHICH NOW HAS AN AVERAGE UNEXPIRED LEASE TERM OF 6 YEARS. OUR PBT CONTRIBUTION FROM MANAGING THE LEASEHOLD DISPOSALS WAS £0.7M IN THE YEAR TO MARCH 2007. AT THE START OF THE CONTRACT, A PROVISION OF £24.4M WAS SET UP FOR DEALING WITH ALL THE SURPLUS LEASEHOLD SPACE, AND THE PROFIT ELEMENT IS RELEASED TO THE INCOME STATEMENT AS LETTINGS ARE ACHIEVED. AS WE HAVE NOW DISPOSED OF ALL THE SURPLUS SPACE OTHER THAN 80,000 SQ FT, WE EXPECT PROFITS TO REDUCE FROM THE CURRENT LEVEL TO AROUND £0.2M NEXT YEAR AND THEN TO RUN OFF COMPLETELY BY AROUND 2010.

ON THE TELEREAL II CONTRACT, WHERE WE MANAGE CERTAIN LEASEHOLD LIABILITIES FOR TELEREAL (ESSENTIALLY RENT REVIEW RISK VERSUS 3% PER ANNUM FIXED INCREASES), WE GUIDED ON AN ANNUAL PBT CONTRIBUTION OF £14M PER ANNUM UNTIL THE BREAK CLAUSE IN THE CONTRACT IN MARCH 2010. AS IT HAPPENS, WE ACHIEVED £16.1M PBT IN THE YEAR TO MARCH 2007 BECAUSE OF TIMING DIFFERENCES, BUT YOU SHOULD CONTINUE TO ADOPT £14M P.A. AS EXPECTED PROFIT FROM NOW UNTIL THE BREAK CLAUSE IN MARCH 2010.

ON LEICESTER GRAMMAR SCHOOL, WE SIGNED A CONTRACT IN JANUARY THIS YEAR WITH A LEADING INDEPENDENT SCHOOL. WE PROVIDE THE FUNDING FOR THE PURCHASE OF LAND AND CONSTRUCTION OF THE NEW SCHOOL. OUR TOTAL INVESTMENT IS £30.5M WHICH IS ACCOUNTED FOR AS A FINANCE LEASE. THE RETURN ON THE FINANCE LEASE IS 5.85%, HOWEVER, IN ADDITION TO THIS WE WILL ALSO RECEIVE A UNITARY CHARGE LINKED TO RPI. THIS GIVES A TOTAL EXPECTED RETURN OF 8.5%. WE HAVE A REITABLE INTEREST IN LAND FOR THE PERIOD OF THE CONTRACT.

Accor hotel portfolio



- Purchase price £439m + £35m capex over 4 years
- 84 year leases with 12 yearly tenant break clauses
- Expected annualised rental income (year 1) £28.7m
- LCCE + insurance £(1.7)m
- Net income £27.0m
- Growth in turnover over 10 years to 2006 +3.9% pa
- Net yield in year 1:
 - If capex discounted to NPV 5.50%
 - Cash basis 5.85%

Geographically diversified portfolio of 30 hotels on turnover rents

OUR ACQUISITION OF THE ACCOR HOTEL PORTFOLIO RELATES TO 30 HOTELS IN THE 2 STAR AND 3 STAR RANGE WHICH WE ACQUIRED FOR £439M WITH A COMMITMENT TO SPEND A FURTHER £35M ON CAPEX OVER THE NEXT 4 YEARS. IT IS MORE THAN A SALE AND LEASEBACK IN THAT WE TAKE RISK ON EXTERNAL MAINTENANCE AND INSURANCE AND, UNDER AN UMBRELLA AGREEMENT, WE ALSO UNDERTAKE TO HELP ACCOR TO SECURE NEW HOTEL DEVELOPMENT OPPORTUNITIES.

AS AT 31 MARCH WE HAD ACQUIRED £290M OF THE HOTELS WITH THE BALANCE TO COME THROUGH SHORTLY AFTER OBTAINING THIRD PARTY CONSENTS.

WE PROJECT A NET RUNNING YIELD IN YEAR ONE OF 5.5% IF THE FUTURE CAPEX IS DISCOUNTED TO A NET PRESENT VALUE OR 5.85% ON A CASH BASIS. RENTS ARE CALCULATED ON AN ANNUAL TURNOVER BASIS AND HISTORIC PERFORMANCE IN TURNOVER HAS BEEN STRONG WITH GROWTH OF 3.9% PER ANNUM OVER THE LAST 10 YEARS. ALMOST 50% OF THE HOTEL ROOMS ARE IN AND AROUND LONDON AND WE EXPECT A POSITIVE IMPACT FROM THE 2012 OLYMPICS.

THE HOTELS ARE MAINLY IN CITY CENTRE LOCATIONS AND, WITH LOW RENT GEARING (RENTS AT AN AVERAGE OF 21% OF TURNOVER), THE VACANT POSSESSION VALUES ARE CURRENTLY IN EXCESS OF INVESTMENT VALUE.

THESE ARE INVESTMENT PROPERTIES WHICH WILL BE REVALUED AT 6 MONTHLY INTERVALS, AND THE MARCH 2007 VALUATION SHOWED A MARGINAL INCREASE PRE-ACQUISITIONS COSTS AND A DEFICIT POST-ACQUISITION COSTS.

Royal Mail

Investment properties and leasehold liabilities on surplus accommodation



Royal Mail – a natural candidate for property partnerships

Freehold Investment Properties

- £97.8m investment property acquisition
- 1.3 million ft² (78% Royal Mail, 17% sublet, 5% vacant)
- 181 properties - average rent for Royal Mail occupation of £3.03 per ft² (below current ERV)
- 15 year leases with 10 year break + 10 year extension right
- Annual rent reviews for Royal Mail at 2.5% pa fixed increase
- Initial rents - £4.87m pa (65% from Royal Mail)
- SIC15 adjusted rents - £5.25m pa

Leasehold liabilities on surplus accommodation

- 1.35 million ft² (74% warehouses) – 113 properties
- 51% vacant, 49% sublet
- 5.7 years average unexpired lease term
- Expect £2.4m profit – c. £0.75m in year 1 declining to £0.25m by year 3 – dependent upon letting success

THE ROYAL MAIL OUTSOURCING CONTRACT IS IN TWO PARTS - A FREEHOLD SALE AND LEASEBACK PORTFOLIO AND THE MANAGEMENT OF SURPLUS SPACE ON A LEASEHOLD PORTFOLIO.

THE SALE AND LEASEBACK PORTFOLIO WILL BE VALUED AT 6 MONTHLY INTERVALS BY KNIGHT FRANK. THESE ARE SMALL PROPERTIES WITH AN AVERAGE LOT SIZE OF APPROXIMATELY £0.5M, MAINLY IN SMALL TOWN CENTRES. YOU WILL SEE THAT THE LEASEBACK RENTS TO ROYAL MAIL ARE EXTREMELY LOW AT SOME £3 PSF, WHICH IS BELOW CURRENT RENTAL VALUES. WE BELIEVE THAT THE PROPERTIES ARE VERY ATTRACTIVELY UNDERPINNED BY VACANT POSSESSION VALUES. SO, WE SEE THE EXERCISE OF THE POTENTIAL BREAK CLAUSES IN YEAR 10 AS A POSITIVE RATHER THAN A NEGATIVE.

THE SURPLUS LEASEHOLD SPACE WAS PRICED AT AROUND £26M. THE PROFIT ELEMENT WITHIN THIS PROVISION WILL BE RELEASED TO THE INCOME STATEMENT AS LETTINGS ARE ACHIEVED SUBJECT TO THE YEAR-ON-YEAR MOVEMENT IN THE NPV OF LIABILITIES. WE GIVE GUIDANCE ON POTENTIAL PROFITS FROM THIS ELEMENT OF THE CONTRACT AT THE BOTTOM OF THE SLIDE.