



## **Gearred Property Update**

### **Whitbread Court Pension Fund**



**Irish Life**

## 1. About the Whitbread Court Property

Whitbread Court is a modern three level office building completed in 1990 totalling 65,983ft<sup>2</sup> (6,130m<sup>2</sup>) with approximately 293 car spaces. The building is located in Houghton Hall Business Park, Dunstable which is close to Luton. The property is arranged in three linked blocks, known as buildings 1, 2 and 3 each providing well specified office accommodation on ground, first and second floors. Extensions linking the buildings were completed in 2001.

The property is let in its entirety to Whitbread Group plc for a term expiring on 12th February 2022 on a full repairing and insuring basis incorporating five-yearly upward only rent reviews. The next review date is due in February 2012.

## 2. Factors impacting the performance of the fund

Source: Irish Life

### Market Overview

Office Markets in the UK continue to be split between Central London and the rest of the Country. Central London with its safe haven status continues to attract overseas and institutional investors. With limited opportunities available, investors are competing aggressively, keeping downward pressure on yields. Outside London and excluding major Cities investment market conditions remain less buoyant overall.

Investor demand remains narrowly focused and the prime/non-prime yield spread remains almost three times higher than at the peak of the boom in 2007.

Key risks to the sector come from debt and a pickup in credit availability continues to look unlikely. Major UK Banks continue to reduce their exposure to the sector; recent reports suggest that

Lloyds bank is due to bring a large portfolio of distressed assets to the market.

In terms of the office occupational market, a lack of development in London and rising demand has but upward pressure on rental levels. Regional occupier demand remains generally weak, due to elevated supply and concerns over the Governments austerity measures. Occupier markets outside of Central London are still generally subdued and rental growth does not appear likely in the immediate future.

### Property Update

Dunstable is a sub-market of the Luton market. A comparable transaction that has taken place in the area is a building in Capability Green, Luton, which is reported to be currently under offer at 7.5% - let to Rexem Beverage Can UK Ltd. with 12 years to lease break and annual rent of stg£780,000 (stg£16.57 psf). The yield on Whitbread Court is currently at 7.5%.

A comparable rental transaction is Gainsborough House, which is located in the same business park as Whitbread Court. This had been marketed for some time by CB Richard Ellis quoting a headline rent of approximately Stg£12.75 per sq ft with a significant rent-free period available to any new tenant. We understand this is now under offer at a lower headline rent of stg£12.50 per sq. ft. along with a rent free period of 3.5 years for a 15 year term with a break at year 10. This evidence suggests that Whitbread court is overrented and that a rent increase at the next review is unlikely.

Rental payments continue to be made in a timely manner by the tenant. Loan interest payments are being easily met with rental income exceeding interest repayments by 1.7 times (i.e. the Interest Cover Ratio is 1.70), helped by current low interest rates. This has allowed capital loan repayments of

Stg£150,000 in the first six months of 2011, reducing the outstanding loan balance.

In June 2011, the amount of the loan outstanding is stg£9,150,449 (stg£7.468m fixed and £1.682m variable) against a June 2011 property value of £11m – LTV is 83%. The loan from Bank of Scotland is for a term of 17.5 years maturing in 2022. The margin on the loan is 1.2%. The fixed rate element of the loan matures in October this year; this will increase the ability to make higher capital repayments estimated at approximately stg£500k per annum, depending on what happens to UK interest rates. The margin on the loan will stay at 1.2%.

Whitbread Group plc continues to perform well through the recession and has embarked on an “expansion” path over the past couple of years with increased acquisitions for their “Premier Inn” and “Costa Coffee” brands.

As well as the refurbishment programme undertaken by the tenant in 2009 and 2010, since the beginning of 2011 the tenant has carried out an extensive cleaning of the exterior of the building. This reflects the commitment of the tenant to the building.

### 3. Looking Ahead

- The property was visited by our asset management team in early 2011 and the building is in extremely good condition following refurbishment.
- As reported in our last communication, the asset manager’s focus has been concentrating on exploring the exit and/or hold strategy of the fund. If the property was sold now at the current valuation of stg£11m it would result in a return to policyholder substantially below the initial investment level.
- Earlier this year the asset manager sought advice on the potential sale of the asset in the current market and its potential in the event we were successful in extending the lease with the tenant. An extended lease would improve the investment value and marketability of the asset. It was also explored whether the tenant themselves would be interested in buying the building. Whitbread felt on balance that it is too early to do anything now. They would only consider a purchase or a lease extension if the deal is compelling for them. They are under no pressure timing wise and they like the fact that the rent is fairly low right now. It is therefore felt that there is too big a distance on numbers for a deal to be done at this time.
- The alternative strategy is to continue to hold the property and to pay as much capital repayments from the excess cash in order that the debt is reduced, particularly with the fixed element of the loan maturing later this year.
- The debt is being repaid quarterly. The capital repayments over the next 12 months are estimated to be in the region of 5% of the loan given the current net asset value. This is of course dependent on what happens to UK interest rates over the next 12 months.
- Timing on the disposal of the property will be determined by debt repayment levels as well as market conditions, property specific issues (particularly the reducing lease term and possibility of extending it) and the availability and cost of refinancing.

## 4. Performance of the Whitbread Court Pension Fund

### Property Valuation – June 2011

This property was purchased in 2004 for Stg£13.3m (plus costs). The value of the property remains unchanged at Stg£11m in the six months to June 2011.

### Fund Return (unit price movements)

#### From 1st January 2011 to 30th June 2011

This valuation and all other factors contributing to the return on the fund such as the outstanding loan balance (Stg£9.15 million), loan interest expense, fund costs, rental income, exchange rate movements and fund management charge has resulted in the value of the units in the fund rising from 0.331 to 0.346 since the last valuation date i.e. 1st January 2011 to 30<sup>th</sup> June 2011.

The value of your plan is in your annual benefit statement and is the current guide value. This guide value also reflects any movements in the fund since the 30<sup>th</sup> June 2011.

## 5. Keeping you up-to-date on your fund

Property valuations are completed in June and December each year. This property update reflects the last property valuation as at 30th June 2011. The accompanying benefit statement reflects an up-to-date value of your investment.

You can call Invesco on 01 294 7600 or contact the Irish Life Property Services Team on 01 704 1831 to get an up-to-date value at any stage on your investment.

In the interest of customer service, we will record or monitor calls.

**Warning: The value of investments may go down as well as up.**

**Past performance is not a reliable guide to future performance.**

**This product will be affected by changes in currency exchange rates.**

The information provided is a guide only and may be subject to change.

The valuation details regarding the asset(s) in question are confidential and should be considered price sensitive information.

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