

# Real Estate Securities Monthly *Europe*



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**1 September 2009**

**EPRA 1,175 • F3REAL 1,948**

**FTSE 100 4,820 • 10 YR Gilt 3.55% • U.K. 10 YR+ Corp Bonds 6.16%**

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Important disclosure on page 4

## Green Street's Notable Changes in Estimates and Opinions\*

### Changes:

Company	Change in EPRA Earnings						NAV Change pence/€	Date of Most Recent Previous Recommendation	Most Recent Previous Recommendation	Opinion Change	
	'09		'10		'11						
	pence/€	%	pence/€	%	pence/€	%					
ProLogis European Properties	PEPR	(€ 0.03)	(5)%	(€ 0.08)	(16)%	(€ 0.05)	(12)%	(€ 0.37)	27-Apr-09	HOLD	↑ BUY
SEGRO	SGRO	(7.5)p	(34)%	(4.3)p	(20)%	(1.5)p	(8)%	(5)p	27-Apr-09	BUY	↓ HOLD

\* Reflects changes since the more recent of last month's publication of the Real Estate Securities Monthly or the last published estimates on any given stock. Commentary does not include modest changes, "normal" fine tuning of estimates, or opinion changes that occurred primarily due to the pricing of a given stock or the pricing of the entire group.

#### ProLogis European Properties

CLa

The PEPR spot NAV estimate calculated by Green Street is herein decreased by 5% to €6.41/sh after an update for 2Q09 financial results. The NAV decline is largely due to a roughly 30 bp increase in the average Net Initial Yield used to value the properties (to 8.6%). The steepest yield increases were implemented for Central Europe (+ 65 to 85 bps), while we recorded minimal changes in Belgium and Germany. PEPR's EPRA earnings have also been reduced. The primary driver of the 16% and 12% declines in '10 and '11 estimates, respectively, is the addition of €375 million of equity to PEPR's balance sheet so as to reduce leverage below 50%. PEPR is currently in the process of changing its corporate structure, which is likely to lead to an equity issuance in late '09 or early '10. While dilutive to earnings (and prospectively to NAV) per share, an equity issuance would greatly enhance enterprise value as it would remove the financial distress cloud that has hung above PEPR for some time. In addition, PEPR is likely to extend its bank facilities and obtain more secured debt, which should serve to refinance its '10 obligations.

Given PEPR's high implied valuation yields and the significant probability that financial distress will be further reduced, we herein increase our recommendation to BUY.

#### SEGRO

CLa

SGRO's spot NAV estimate as calculated by Green Street is herein lowered by 2% to 315p/sh in order to reflect the closing of the Brixton acquisition as well as the recent £250 million share placement. SGRO's EPRA earnings estimates are also herein reduced. The main driver is a 1H09 loss on the sale of trading properties and our current expectation that no profit will be generated by this segment over the next 18 months. This contrasts with a previous expectation of profitability. We herein downgrade the shares of SGRO to HOLD. While SGRO's valuation seems reasonable versus the U.K. majors (low premium to NAV, relatively high implied valuation yields), PEPR represents a much more compelling risk/reward trade-off within the European industrial group.

Analysts: John Lutzius (JL) is primary analyst on BLND, HMSO, LAND and LII. Cedrik Lachance (CLa) is primary analyst on PEPR and SGRO.

1-Sep-09 ▪ EPRA 1,175 ▪ F3REAL 1,948 ▪ 10 YR Gilt 3.55% ▪ U.K. 10 YR+ Corp Bonds 6.16%

Symbol	Recent Price	Out. Shares Millions	Market Value Millions	Debt		GSA Spot NAV	Observed		Prem/(Disc)		Opinion
				Lev. Ratio (1)	Net Debt /EBITDA (2)		Prem/(Disc) to		Warr. Share Price	to Warr. Share Price	
							GSA Assets	GSA NAV			

**U.K. Majors**

BRITISH LAND	BLND	471p	854	£4,019	60%	9.8x	384p	9%	23%	499p	-6%	BUY
HAMMERSON	HMSO	390p	697	£2,717	50%	8.2x	341p	7%	14%	389p	0%	HOLD
LAND SEC.	LAND	612p	755	£4,617	52%	8.6x	539p	6%	13%	598p	2%	HOLD
LIBERTY INTL.	LII	505p	577	£2,912	69%	10.6x	296p	22%	70%	416p	21%	SELL

**U.K. Majors Average**

57% 9.3x 10% 28% 4%

**European Industrials**

PROLOGIS EUR.	PEPR	€3.83	191	€730	60%	7.4x	€6.41	-16%	-40%	€4.04	-5%	BUY
SEGRO	SGRO	339p	734	£2,492	55%	11.3x	315p	3%	8%	346p	-2%	HOLD

**European Industrials Average**

56% 10.5x -1% -2% -3%

Property Type (3)	Geographic				Like-For-Like Net Rental Income Growth				End of Year Occupancy (Like-for-Like Portfolio)								
	Retail			Office		U.K.		Continent		'09		'10		'11		'12	

**U.K. Majors**

BLND	59%	39%	0%	96%	4%	-2.1%	-2.4%	-1.8%	0.1%	95.0%	93.4%	93.5%	94.9%
HMSO	85%	15%	0%	66%	34%	-2.4%	-2.0%	-1.6%	0.5%	94.3%	93.3%	93.4%	95.8%
LAND	58%	39%	0%	100%	0%	-3.7%	-4.6%	-2.6%	-0.4%	92.4%	91.4%	91.3%	93.1%
LII	85%	10%	0%	94%	0%	-4.2%	-3.1%	-1.6%	0.7%	95.1%	92.9%	94.0%	95.8%

**U.K. Majors Average**

-3.1% -3.2% -2.0% 0.1%

**European Industrials**

PEPR	0%	0%	100%	17%	83%	-2.1%	-3.5%	-1.8%	0.6%	94.1%	92.6%	93.1%	95.1%
SGRO	1%	13%	86%	71%	29%	-3.7%	-4.4%	-2.5%	0.4%	87.3%	85.8%	86.3%	88.3%

**European Industrials Average**

-3.4% -4.2% -2.3% 0.5%

Net Initial Yield (4)	EPRA Earnings								Dividends					
	Economic Cap Rate (4) (5)				Estimate				Growth		Yield		'09 Dividend	Cover From '09
	GSA	Implied	GSA	Implied	'09	'10	'11	'10	'11	'10	'11	Yield	Earnings	

**U.K. Majors**

BLND	7.2%	6.6%	6.5%	5.8%	25.2p	23.9p	26.7p	-4.9%	11.6%	5.1%	5.7%	5.5%	1.0x
HMSO	7.0%	6.6%	6.1%	5.7%	18.8p	16.4p	14.5p	-12.8%	-11.5%	4.2%	3.7%	3.9%	1.3x
LAND	7.9%	7.4%	6.8%	6.4%	38.9p	33.8p	35.5p	-13.0%	4.9%	5.5%	5.8%	5.7%	1.1x
LII	7.2%	5.9%	5.4%	4.4%	19.8p	19.6p	18.5p	-0.9%	-5.6%	3.9%	3.7%	3.3%	1.2x

**U.K. Majors Average**

6.3% 5.7% -8.2% 1.5% 4.8% 4.9% 4.8% 1.1x

**European Industrials**

PEPR	8.6%	10.2%	7.8%	9.3%	€0.61	€0.42	€0.36	-29.9%	-16.0%	11.1%	9.3%	0.0%	n/a
SGRO	8.3%	8.1%	6.9%	6.7%	14.6p	16.9p	16.9p	16.2%	-0.2%	5.0%	5.0%	2.5%	1.7x

**European Industrials Average**

7.1% 7.2% 6.9% -3.4% 6.2% 5.9% 2.0% 1.4x

All averages are weighted by market cap.

BLND & LAND have 31 March financial year ends whereas HMSO, LII, PEPR & SGRO are as at 31 December. The years shown correspond to the most recently completed calendar year (e.g. '09 refers to the financial year completed 31 March 2010 for BLND & LAND and 31 December 2009 for HMSO, LII, PEPR & SGRO).

(1) Total Liabilities (Market value, net of cash) / Total Assets.

(2) Net Debt (Book value of debt, net of cash) / '09E EBITDA.

(3) Based on GSA spot of asset values.

(4) For stabilized investment properties only (i.e. excludes recent developments in lease-up)

(5) An economic cap rate adjusts for costs incurred by the landlord that are not accounted for in traditional real estate yield measures and is more comparable to capital market benchmarks. As compared with a U.K. net initial yield, an economic cap rate subtracts operating costs not reflected in net rent (which can be a sizable burden when vacancy is high or properties are operationally intensive), leasing commissions, and a structural cap-ex reserve. Economic cap rate is calculated without adding purchaser's costs to the denominator. As compared with a U.S. nominal cap rate, an economic cap rate subtracts tenant improvements and leasing costs, and a structural cap-ex reserve.

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