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(Interview of September 8, 2004)

Brixton PLC

LSE:BXTN

Tim Wheeler
Chief Executive Officer

Brixton plc is a leading player in the UK real estate market and is listed on the London Stock Exchange. It owns or manages around 18.6m sq ft of industrial, warehouse and business space around London in the South East and Manchester in the North West. Its holdings include more than 4m sq ft of space close to Heathrow Airport - where rental values for industrial property are the highest in the world. Brixton produces results by focusing on a successful acquisition and development programme, effective asset management, customer service and strategic joint ventures. This approach is underpinned by an innovative financial strategy which gives Brixton flexibility, a competitive advantage and an investment-grade credit rating. The company operates through two principal subsidiary companies. Brixton Investments is responsible for acquisitions, disposals, leasing and development. B-Serv is the customer service-focused manager of property owned by Brixton and its joint ventures, Equiton and Heathrow Big Box. As the UK Government considers introducing taxation measures conducive to the formation of Real Estate Investment Trusts, Brixton's sector specialisation and existing focus on income distribution has led it to be tipped as being one of the most suitable companies for potential conversion.

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Tim Wheeler, Chief Executive Officer, spoke with *Wall Street Reporter Magazine*, on September 8, 2004.

WSR: For those members of our audience that haven't had the opportunity of tracking Brixton plc and its

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history, let's start with an overview and timeline of the company.

BXTN: We are one of the larger UK plc property companies. We have a portfolio of about 18.6 million square feet of space worth just over 1.7 billion pounds. We own approximately 80 industrial estates. We predominantly focus in the industrial and warehousing sector, and most of our activity is in the southeast of England, concentrating on the western half of the home counties. In effect, the London to Heathrow axis. The portfolio is 90% industrial and all but 7% of it is in the southeast.

WSR: Can you give us a sense here of what you see that market opportunities are aligned here in those segments that you are focusing on?

BXTN: We have become the leading specialist in this market that I have just described. Most of the other UK companies are multi-faceted or much smaller. We, over the last seven or eight years, have deliberately driven into the distribution, logistics and the industrial market. Industrial is a bit of a misnomer in the UK and certainly in the southeast because it doesn't tend to be heavy industry at all. It is predominantly service support space and throughput distribution. We've focused on this market because perversely, the Thames Valley and West London, are

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one of the few parts of the commercial market in the UK that actually shrunk in supply size. It's reduced in size over the last 20 years because competing land users have demanded that the uses of these industrial and warehouse sites have gone to offices then to leisure and out-of-town retail and now to what our government calls brownfield residential, in other words, building more of the houses that the country needs on old industrial sites. Now, this may sound odd, but obviously, we are buying into the market where the supply side is therefore automatically shrinking with generally the demand side being enhanced because of the way that operators use the space. The Americans have a good term for it, flex space, and that's really what a lot of our distribution is about. And therefore, we've been able to take advantage of the increased demand for more flexible accommodation in the market in which we operate. The results of that is that we've tended to outperform our peer group on a share performance basis and a net asset value growth basis over the last few years since we exited the various markets that we operated in before. It may be useful for your listeners and readers to know that Brixton was formed in the 1920s, floated in 1935, and up until seven years ago, we operated in six countries: the US, Australia, Germany, France, Belgium, and we'd exited

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Holland some time before that, as well as the UK. We also operated across the commercial sectors: office, industrial and retail. We have now sold out of those locations and have become very concentrated on the market I have described.

WSR: The company does operate through two principal subsidiary companies, can you give us a sense of those subsidiaries and their focus?

BXTN: We split the business in two, the sort of traditional property investment holding company is Brixton Investments and we also have another company called B-Serv. B-Serv is effectively a manager for Brixton and its joint venture partners. And the thing we concentrate on over here, which is probably more prevalent in the States because leases tend to be shorter, is customer service management. In the UK, with a historically typically longer lease structure, landlords have been absent in customer relation management so what we decided we would do is try and provide our tenants, our customers, with better services on the estates that we manage. Our industrial estates tend to be larger in size. The average lot size outside the joint ventures - which, particularly in the case of Equiton, tend to concentrate on smaller properties - is more than 30 million pounds. They give us the

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opportunity to both physically and financially manage a critical mass, enable us to provide proper security and servicing of those estates. And the driver that we've seen has been to increase the quality of those services and reduce the cost. Brixton, because of its expansion into this market, has bought something like 70 of these estates in the last five years, each with its own management regime that needed to be consolidated. B-Serv, the company we formed to do this, has now gone on to offer tenant services and the desire for that from our occupier base is really to help them out with the repairing liabilities. We've done this effectively by using our supply chain which we've got anyway because we have so many buildings to refurbish and re-let. We can offer to upgrade the premises which of course, they are covenanted to do under the terms of their full repairing leases in the UK. There's a double benefit: they get the job done effectively, and it takes the hassle out of them having to look after their properties and we get our buildings enhanced. And what we've been about doing is trying to increase our retention level with more of our tenants staying by virtue of the fact that we're more responsible landlords. The proof of this is really the customer satisfaction surveys that we've commissioned, which have increased satisfaction pre-B-Serv, which was

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formed in 1999, where about half our tenants were satisfied and half were dissatisfied, to over three-quarters are now happy with this service. And this year alone, in all the lettings that we've done, more than 60% of them - not lease renewals with existing tenants - in these new situations have been done within our existing customer base which now totals more than 800 companies.

WSR: Is there anything we should note there about your acquisitions or joint venture restructurings?

BXTN: I think the important thing is, to put in terms of the context, we've become the market leader in the Heathrow market. Heathrow has the highest industrial land values in the world. There is a reason for that. It's scarcity of land, it's the constraints of the planning system, and it's the fact that Heathrow remains one of the most dominant airports in the world. To put it into some sort of context, it's now third in Europe in passenger number size, but most importantly, within the UK, it's responsible for more airfreight than all the other UK airports put together. And rather uniquely, nearly all the airfreight - 93% of it - is carried in the underbelly of passenger planes. And Heathrow is an airport that actually flies to more destinations in the world than any other airport. So, the sourcing of goods is paramount for the UK

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as it has now become more of an assembler of goods with other people's raw materials and products than a manufacturing country in itself. The key to what we do is to dominate the Heathrow market. We've gone from owning really very little stock there to becoming probably the largest owner. The Heathrow market is very important to us although we have some of the holdings now in a joint venture - Heathrow Big Box with the Prudential. These are more static, primer, perhaps drier investments, and we are repatriating cash through this restructuring into more development and income-enhancing opportunities. About 60% of our portfolio is in West London including Heathrow and it's a market that we have now seen expanding again as passenger numbers and cargo growth has come back to where it was pre-9/11 and more importantly, is now substantially growing.

WSR: What are the things we should note about the recent performance? And what are some of the other key drivers here that are attributing to your success?

BXTN: The key measures for the UK property investment company model, are two things. One is NAV, net asset value growth. We've produced 7% in the half year or about 11%, June to June. This is impressive compared to all the other companies over here, most of whom have had the benefit of

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having retail portfolios, retail being the best performer in the UK with the consumer boom for the last couple of years. It's particularly pleasing that having had no retail exposure, we still managed to beat the peer group on that latest NAV enhancement. We did a share placing earlier in the year, which is quite unusual in our sector and that has had an effect indeed of diluting slightly that NAV growth, that would have been 1.5% better had that not taken place. We've also had some very impressive profit before tax enhancements of nearly 52%, but the second measure of the real stability of growth is investment profit which is really recurring profit excluding the exceptional. But there again, we were over 5% up on the half-year. Our figures beat consensus market forecasts. We have done this now in the last couple of occasions and we think it goes back to being a specialist and having this customer focused approach. We've also, in recent times, expanded up into the Manchester where we had a small holding previously. It was the only place outside the southeast where we were represented, and we brought a large chunk of an estate called Trafford Park, which is allegedly the first industrial estate in the world. Trafford Park is next to the Manchester United football ground, and we brought 2.7m square feet in 200 units, in March. On the lettings that

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we've achieved since March, we've seen an enhancement over the estimated rental value of over 13%, which is impressive given inflation levels as low as they are in the UK at the moment. We also saw a valuation surplus after costs of 1.5% March to June, which again is very pleasing. So, we are remaining a focused company by buying more property that needs management-intensive activity through B-Serv

WSR: As we look out at these performance numbers, what we should note about these numbers? Are they sustainable going ahead?

BXTN: The underlying aspect of the business that we think we can control or try and control is rental growth. If we don't have tenants we can't have income growth, and we don't really have a booming business. The UK is seeing a fairly extraordinary period in terms of investment demand for property because, first of all obviously, the downturn post-dotcom boom in equities, but more recently, there has been a stalling in the equity market, and bonds have produced negative returns so the asset allocators of the big institutions have been very keen to get the relative yield benefit of property. There has been a huge weight of money coming into properties this year, which has driven down equivalent yields on our portfolio by about 20 basis points to 6.8%. Last year was really the start of the

renewed tenant demand and the start of proper rental growth again. So, over 12 months to June, we've seen 2.6% rental growth in our industrial portfolio. The industry benchmark over here demonstrated 0.6%, so we've obviously done much better than that. However, we are sounding a note of caution: for capital value growth to continue the way that it has, yields must fall even further and our only concern about that is that with the rising interest rates, with the institutions already chasing yields down to historically low levels, with the potential slowdown in the global economic recovery, and some domestic issues like slowdown in consumer spending and a fall in house prices which underpins so much of the UK economy, we just think it's probably less likely that yields will continue to fall uniformly. We base our business around enhancing our income from our portfolio which is something we have more control rather than the sentiments that drive the investment yield.

WSR: Is there anything we should note about Brixton's joint venture strategy, which separates it from the rest of the peer group?

BXTN: We were one of the first companies over here to get into limited partnership structures. We've always been very clear that the difficulty is that you can create conflict, which may ultimately not please either your

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stockholders or the people that have taken stakes in your ventures. We've either done them on a site-specific basis as we have done on two of our more dry prime assets at Heathrow Big Box with the Prudential that I described earlier. We set up this 50% partnership with them this year, but that's ring-fenced just to deal with those two properties. Also, in 1999 we set up a smaller properties fund called Equiton which now has two other partners - one of them also now happens to be the Prudential and the other is Equitable Life. This has become basically the repository for all Brixton's smaller sub-15 million pound industrial estates. We've sold probably about 20 estates into that vehicle and brought at least another 20 more. That fund now has over 3 million square feet of smaller southeast industrial worth about 300 million pounds. It has consistently produced total returns well in excess of the benchmark. We have the ability to gear these vehicles up more highly than we could do on our own balance sheet which enables us and our partners to participate more actively in the upside of the performance. It also gives us the opportunity to charge performance fees providing of course that performance comes through. So, we make these joint ventures distinct, we gear them up more aggressively than we could do on our book, and we try and encourage our

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institutional partners to invest in them because of that performance record.

WSR: What are the things that we should highlight in closing about Brixton PLC of today and the Brixton PLC of tomorrow?

BXTN: I think we've basically set our stall out to do one thing and do one thing well, which is industrial in the UK. And to reiterate when I say "industrial", of course, I do mean warehousing and business space as well. We are very much on track now to continue to be the market leader in that. We can't sit back; we need to grow the company and we have to continue to look at new opportunities. All our finance is now unsecured, which gives us the opportunity to act very quickly. We have a reputation for fair dealing and getting on with our business. We've called the market correctly in terms of the slowdown three years ago in occupational demand, the restart of our development program at the turn of this year, and we are now saying that whilst we are very confident that we can continue to outperform, we would just caution as to whether with the likely modest levels of rental growth going forward, capital values will continue to grow as strongly. So, what we see is a good environment, but it's just one that we have to keep a slight eye on because the investment market is certainly

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expecting levels of rental growth that might not come through, which might then affect the total returns of some of those organizations that have been paying recent prices. Now, the flip of that is that we've deliberately de-gearred into this market to take advantage of any sales that come through in anticipation of that change round in sentiment. In the UK, as I'm sure you are aware, the government, the property industry and the individual companies have been consulting over the introduction of tax transparent vehicles. They are called Property Investment Funds over here, but we much prefer to call them REITs. There is obviously a weight of expectation in our markets in anticipation of the legislation that we think will come through within the next 6 to 12 months. That will have a fundamental change for our business and in our one or two recent trips to the States to see existing shareholders or indeed talk to potential shareholders; there is clearly a lot interest in the UK property scene because of this potential change of legislation. Salomon Smith Barney has named Brixton as probably the most "REIT-able" company because we are focused, management intensive, we already distribute a high dividend, we are not aggressively geared, and we are not over-reliant on development. There are some great opportunities and just a slight note of caution.

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However, Brixton remains in a strong relative position and we aim to continue to create shareholder value.

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