

# GP Office Investment

## Extracts from the Business Review

### About GP Office Investment

GP Office Investment, a wholly-owned subsidiary of ABC Investment plc, is a fund manager specialising in commercial offices in the United Kingdom. It manages four funds, incorporating:

- £3.75 billion of assets under management as at 31st December 2009
- 7.4 million square feet of Net Lettable Area
- 160 multi and single-let properties providing office space to 382 occupiers
- an asset allocation of: 45% West End Offices, 35% City Offices and 20% provincial Business Parks

### Strategic objectives

ABC Investment has set the following strategic objectives to guide its five year strategy across all areas of investment activity, including equities and real estate:

1. Increase value of assets under management
2. Achieve a superior rate of return on investment for our clients
3. Maintain a strong brand identity with an emphasis on market innovation
4. Maintain strong relationships with key stakeholders

### Key sustainability impacts on strategic objectives

We have identified three over-arching sustainability issues that are material to the achievement of the group's strategic objectives and which take into account both the long-term drivers of performance and our role as a responsible fund manager. Each of these issues and their corresponding impacts are described below.

In order to determine which issues are material, each year we assess a broad range of sustainability issues for the magnitude of perceived risk and opportunity they present to the business (in financial, reputational, operational and physical terms) and the level of investor and occupier interest, gauged through direct consultation.

## 1. Changing occupier requirements

Meeting the evolving requirements of occupiers is essential if we are to maintain high occupancy rates and protect rental income – even more so in challenging market conditions. As occupier demand patterns change to incorporate a growing concern for sustainability issues, so too must our response. Research by the European Commission found that 84% of international occupiers believed sustainability would be critical to their business in 2009. We continue to observe a similar trend with increasing demand for 'green buildings', particularly from occupiers who wish to align their real estate occupation strategies with their corporate responsibility commitments. As a demonstration of this trend, sustainability was cited as an important factor in 76% of lease renewals we renegotiated in 2009.

We believe there is significant market potential for green buildings. These are deemed to be assets which incorporate a broad range of sustainability factors into their design and are able to operate with minimal impact on the environment, whilst enhancing the socio-economic fabric of their respective localities. Not only are sustainable assets more marketable,

but also there is emerging evidence to suggest that sustainable buildings maintain market level rents and capital values more effectively than less sustainable alternatives. To capitalize on this opportunity, we continue to acquire properties with strong sustainability credentials, including those with externally verified building ratings.

Whilst building ratings alone do not deliver sustainable buildings – indeed, evidence suggests that there is not always a direct correlation between the building rating attained and actual performance in relation to energy and water efficiency – we recognize their role in ensuring a more complete approach to sustainable design. It is for this reason that we participate in other asset specific and portfolio-wide sustainability benchmarks to provide a more rounded perspective on our performance relative to peers. For instance, over 65% of our assets scored above the survey average in Jones Lang LaSalle's The Third Dimension risk profiling survey.

The provision of adaptable, flexible and durable buildings with change in use potential is also an important occupier concern. These buildings are less likely to suffer obsolescence and are more responsive to changing work patterns in increasingly wireless and virtual office environments. More flexible and technology-driven occupation requirements present both a risk and opportunity to future rental income. Through targeted capital investment in adaptability and flexibility we aim to increase the life expectancy of assets under ownership. In doing so, we have maintained steady void rates even in challenging economic conditions. We also recognize the importance of a diversified portfolio, not only to meet occupier demand but to reduce exposure to property market fluctuations. Many of our assets therefore contain a mix of potential uses.

## 2. Weather vulnerability and climate change risks

According to the most recent projections, climate change has the potential to impact materially our ability to deliver strong investment returns, through increased maintenance costs and rising building insurance premiums, where we are wholly or partially responsible for these costs. There are also potential impacts on net asset values through extreme weather events such as flood and storm damage. Since 2004, the number of extreme weather related insurance claims has increased by 40% to 14, with total claims amounting to over £300,000. To protect asset value, we recognize that our acquisition strategy must factor in the immediate and longer term physical impacts of climate change and the risk to buildings that are not protected. This includes disposal of assets which are considered a high flood risk. Since 2004, we have reduced the number of our assets of this type from 11 to 6.

## 3. Resource availability and use

The instability of commodity markets which supply non-renewable fuels (coal, oil and gas) and the prospect of increasing water shortages may place a strain on the price and availability of these resources. We need to take action now to reduce risk exposure to market spikes which can impact on our operating costs and ultimately render buildings obsolete where the cost of retrofitting may not be commercially viable.

The business case for investing in energy efficiency is compelling considering we spend around £20 million per year on energy. Where we have an influence over energy efficiency in our assets, we are committed to implementing all 'low' and 'no cost' measures. Where investment is more significant we require payback within three years. In 2009 our investment in energy efficiency measures totalled £1 million and provided an estimated £2.4 million in energy savings. We project similar investment and savings over the next three years.

In addition to the need to invest in energy efficiency, there is also likely to be higher incidence of obsolescence for buildings which do not meet local energy regulatory standards or occupier needs. Taxes and fiscal penalties levied on carbon emissions may also reduce asset value. We therefore continue to prioritize energy monitoring in light of the rapidly growing carbon market – most immediately in preparation for the Carbon Reduction Commitment Energy Efficiency Scheme in the UK which we estimate will require payment of around £1.6 million in 2011. This payment will be recouped through increased service charges.

In relation to the production and use of waste arising from our asset management activities, we are focused on reducing our exposure to rising costs. As the cost of disposing of waste to landfill outstrips the cost of recycling or reuse, the business case for alternative waste disposal routes is clear. For the assets where we are responsible for waste management, we saved £540,000 in 2009 by diverting waste from landfill, and estimate that savings will rise to £910,000 by 2012.

## The Connected Performance Report

The Connected Performance Report provides a forward looking perspective on the actions taken to manage risks and opportunities associated with the three sustainability issues identified, and the impacts on both financial and non-financial performance. In some cases, the direct financial cost is not material at present. However, we believe that a failure to factor in these issues now has potential to undermine future performance.

While the information provided focuses on areas in which we have either direct managerial or financial control, we continue to work with our occupiers to influence their behaviour towards more sustainable occupation practices. We also manage issues other than just those deemed material and further detail on these can be found in our Sustainability Report.

Where appropriate we have also made references to the Global Reporting Initiative (GRI) Sustainability Reporting Guidelines to ensure alignment with good practice reporting standards.

The Connected Performance Report

# 1. Changing occupier requirements

To ensure that we maintain high occupancy rates we must foster strong relations with our occupiers by responding to both their growing demand for green buildings and their requirements for innovative fit-outs which are flexible to changing work patterns.

Action and outcome	Performance
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**Occupier satisfaction**

Offices which meet the needs of occupiers enable them to sustain their productivity, thereby contributing to the economy and society.

Through post occupation evaluations carried out at newly let premises or following lease renewal, we survey occupiers annually on satisfaction levels associated with key aspects of property management as well as the perceived value of our sustainability efforts. We have also begun to seek feedback from occupiers on sustainability issues during post occupation evaluations, including the importance of sustainability factors in new lettings and lease renewals.

Occupier satisfaction Index scores (out of 5)

	2007	2008	2009
Communication	3.71	3.69	↑ 3.73
Responsiveness	3.74	3.74	↑ 3.76
Understanding needs	3.81	3.84	↑ 3.85
Overall satisfaction with property management team	3.72	3.80	↑ 3.82
Occupied space flexible in use	3.54	3.53	↑ 3.57

**Building ratings**

Assessing our buildings using ratings and benchmarks enables us to prioritize and target sustainability improvements across the portfolio.

Sustainability ratings are considered in the asset appraisal process conducted prior to acquisition. We believe that ratings such as BREEAM, LEED and Energy Performance Certificates provide a useful tool to assess and benchmark sustainability credentials. We also utilize them in design and construction of refurbishments rather than having to incur cost later to retrofit.

We continue to use appropriate benchmarks and risk profiling tools from other sources to complement sustainability ratings. These help to inform asset acquisition and disposal and sustainability improvements.

Value of assets by BREEAM rating

BREEAM 2008 rating*	Value of Assets – BREEAM Offices (£m)
Outstanding	20
Excellent	80
Very Good	80
Good	200
Pass	20

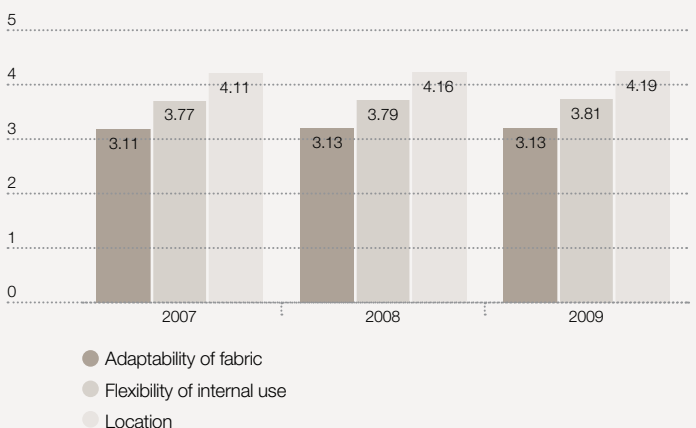
\* Including both 'design-stage' and 'post-completion' assessments

**Adaptable buildings**

Adaptable and flexible buildings that are suitably located are more inherently sustainable as they typically have longer useful lives.

Our investment strategy seeks out assets which demonstrate these characteristics, have a low likelihood of functional obsolescence over the life of ownership and consequently have lower rates of depreciation. We see this as an important future determinant of asset value, as such buildings typically require less investment to cope with changing use. They are also likely to maintain their rental value more robustly and reduce void time during occupier changeover. Our flexible approach to building fit-out ensures that lighting, heating, cooling and interior space designs are adaptable for wide-ranging occupier requirements.

Fit for purpose assessment (1 = low 5 = high)



## Commentary

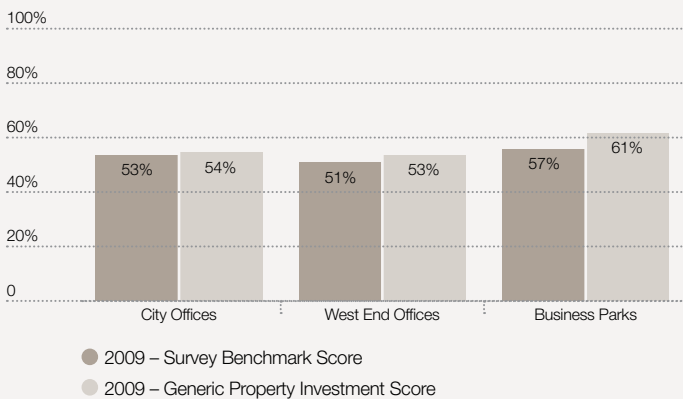
### Sustainability and new lettings/lease renewals

	2007	2008		2009
Total value of new lettings and lease renewals (£m)	20	12	↓	8
New lettings and lease renewals where sustainability cited as an 'important' factor (%)	59	63	↑	76

Our occupier survey results show that we continue to demonstrate strong performance across a broad range of occupier satisfaction measures. In particular, feedback suggests that our offices accommodate changes in use and that we are able to respond to evolving occupier requirements quickly and with minimal disruption.

Since 2007, the number of lettings where sustainability has been cited as an 'important' factor has increased, reflecting growing concern for issues such as energy and material specification amongst occupiers.

### Jones Lang LaSalle's Third Dimension Sustainability Risk Profiling

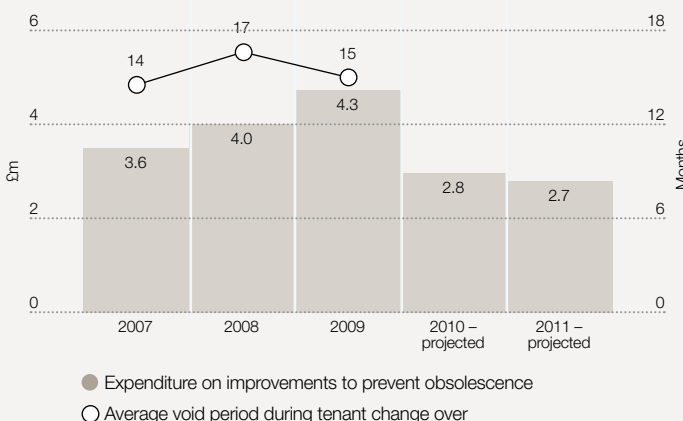


Around £180 million of our most recently constructed developments (by current value) are certified to the BREEAM standard at 'Very Good' or higher.

For existing assets, we use alternative assessments such as Jones Lang LaSalle's The Third Dimension survey which analyses the sustainability risk profile of over 2,000 properties. For the property types we own and manage, our score was higher than the survey average score in all three asset classes. This suggests that our portfolio has an inherently lower sustainability risk profile than that of our peers.

We believe that presenting our performance in respect of both of these assessments has marketing advantages that will become increasingly important. Indeed, evidence from the University of California, Berkeley has shown for the first time – with a statistically significant sample – that green buildings command higher rental rates and even higher rental premiums than otherwise identical buildings. We aim to present evidence to reinforce this important finding in our next Connected Performance Report.

### Expenditure on asset improvements



To assess whether our assets are 'fit for purpose' we have developed a methodology which scores buildings against three criteria. By measuring these independently on an annual basis we are able to determine the extent to which our assets are becoming more or less fit for purpose. In addition, we are exploring the link between the fit for purpose score and both the capital value and the rental income.

Ongoing expenditure to prevent obsolescence of our existing assets continues to fall, following significant capital investment which we believe will reduce the rate of depreciation over the life of the building. However, we also acknowledge the impact of market cycles on void periods and will continue to explore the relationship between this and depreciation so that we understand and are able to articulate the correlation more robustly.

## 2. Weather vulnerability and climate change risks

Climate change poses a physical threat to assets under ownership through flooding, storm damage and subsidence. Ensuring that assets are future-proofed for extreme weather events may help protect long-term asset value and reduce both tax and insurance liabilities. It also differentiates our acquisition strategy from that of our competitors, providing us with a more targeted investment pool from which to select assets.

Action and outcome	Performance
<p><b>Climate change adaptation</b></p> <p>Assets which are protected against climate change enable business continuity during extreme weather events, as well as safeguarding human comfort and health.</p> <p>We are implementing a Climate Adaptation Strategy to ensure our acquisition and disposals account for the risk that extreme weather events might pose to future asset value. With the help of climate change modelling techniques, analysing our portfolio provides a method for evaluating the risk associated with owning assets in locations where extreme weather can physically affect an asset, for example, through flooding, storm damage or subsidence.</p>	<p><b>Extreme weather risk</b></p> <p>Weather related insurance claims* (£m)</p> <p>No. of extreme weather related insurance claims</p> <p>No. of assets at high risk of flooding**</p> <p>* In respect of assets where we are responsible for insurance</p> <p>** Greater than 1 in 100 chance of river flooding each year – based on Environment Agency assessments</p>

## 3. Resource availability and use

Energy, water and waste are significant operational costs for our business. As availability diminishes and regulatory controls increase, the cost of procuring these resources also increases, which can make our service charge less competitive.

Action and outcome	Performance																																
<p><b>Energy efficiency</b></p> <p>Reducing energy consumption also reduces greenhouse gas emissions – the cause of climate change.</p> <p>Monitoring our energy use remains a key priority for our business – particularly in light of the forthcoming Carbon Reduction Commitment (CRC) Energy Efficiency Scheme. For assets where we purchase energy on behalf of our customers, our objective is to pass on cost savings from efficiencies to occupiers via reductions in service charges. As part of our carbon reduction strategy, we are targeting the installation of smart meters across our portfolio to improve measurement and monitoring capabilities. We also continue our programme of energy audits to ensure that our building management systems are being used to their full potential and that obsolete plant and machinery is being replaced with more energy efficient alternatives where appropriate.</p>	<p><b>Investment in energy efficiency [GRI EN30 – Partial]</b></p> <table border="1"> <thead> <tr> <th>Energy efficiency investment</th> <th>Total spend in 2009 (£m)</th> <th>Average payback</th> </tr> </thead> <tbody> <tr> <td>No cost</td> <td>0.00</td> <td>Immediate</td> </tr> <tr> <td>Low cost*</td> <td>0.15</td> <td>11 months</td> </tr> <tr> <td>Capital expenditure</td> <td>0.85</td> <td>36 months</td> </tr> </tbody> </table> <p>* Investment in individual projects that are less than £100,000</p> <p><b>CO<sub>2</sub>e savings and Carbon Reduction Commitment Energy Efficiency Scheme liability [GRI EN18 – Partial]</b></p> <table border="1"> <thead> <tr> <th>Energy efficiency investment</th> <th>2009</th> <th>2010</th> <th>2011</th> <th>Projected 2012</th> </tr> </thead> <tbody> <tr> <td>CO<sub>2</sub>e saving (tonnes)</td> <td>6,732</td> <td>6,500</td> <td>6,500</td> <td>6,500</td> </tr> <tr> <td>Equivalent energy saving (£m)</td> <td>2.4</td> <td>2</td> <td>2</td> <td>2</td> </tr> <tr> <td>CRC liability (£m)*</td> <td>n/a</td> <td>n/a</td> <td>1.55</td> <td>1.55</td> </tr> </tbody> </table> <p>* CRC liability will affect cash flow for one year but will be recovered from occupiers. Liability costs based on £12 per tonne of CO<sub>2</sub> and estimated carbon emissions in 2011 and 2012.</p>	Energy efficiency investment	Total spend in 2009 (£m)	Average payback	No cost	0.00	Immediate	Low cost*	0.15	11 months	Capital expenditure	0.85	36 months	Energy efficiency investment	2009	2010	2011	Projected 2012	CO <sub>2</sub> e saving (tonnes)	6,732	6,500	6,500	6,500	Equivalent energy saving (£m)	2.4	2	2	2	CRC liability (£m)*	n/a	n/a	1.55	1.55
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### Commentary

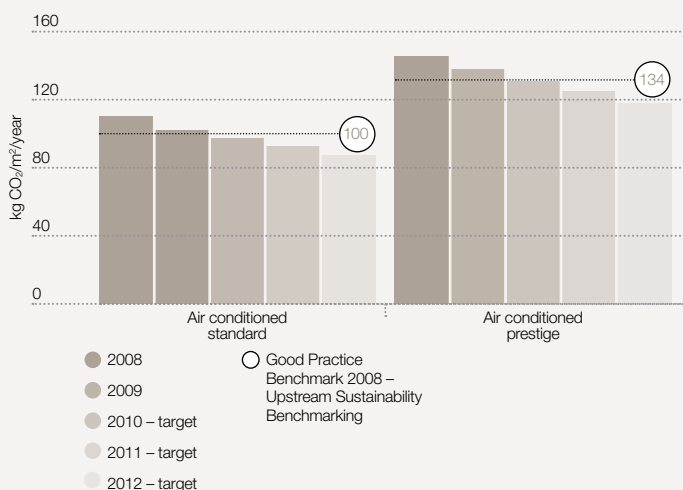
2004	2005	2006	2007	2008	2009
0.27	0.30	0.27	0.28	0.31	0.33
10	12	9	11	12	14
11	11	10	9	7	6

We have incorporated weather risk assessment into our asset appraisal process. The business case for doing this is strong – the cost of insurance claims related to extreme weather in 2009 was just over £300,000. We therefore continue to reduce the number of assets under ownership that are classed as high risk, particularly from flooding.

We are also planning an adaptation programme to retrofit existing buildings with technologies that will reduce the risks of damage from extreme weather.

### Commentary

Whole building (landlord + tenant) energy efficiency  
kg CO<sub>2</sub>/m<sup>2</sup>/year



Emissions from energy consumption totalled 129,984 tonnes of CO<sub>2</sub> in 2009. We monitor and target carbon efficiency in our existing assets and our efficiency continues to improve by approximately 5% per annum across various office types. This is achieved mainly through low and no cost efficiency measures, such as the optimisation of Building Management System control settings and replacement of old energy inefficient lights, but also through targeted capital investment. Our targets will ensure that we exceed Good Practice Upstream Sustainability Benchmarks by 2010.

Our corporate commitment is to reduce landlord and tenant CO<sub>2</sub> by 20% by 2012. This will involve active engagement with occupiers to ensure that they are implementing energy efficiency practices within their own demise. In doing so, we hope to recoup our CRC Energy Efficiency Scheme carbon credit bonus of 10% and 20% respectively in 2011 and 2012 for high performance in the league table.

## Action and outcome

**Water efficiency**

Water is a valuable natural resource which is scarce even in the UK. Reducing consumption therefore lessens the strain on fresh water supply.

Water is an emerging concern, and one that we believe will increase in importance over time as regulatory controls on supply and demand become tighter. By fitting water saving devices and closely monitoring consumption levels, we continue to target water efficiency improvements in the common parts of our managed assets. Our investments are typically low or no cost, and savings are passed on to occupiers once the initial expenditure has been recouped. We also engage with occupiers to encourage water efficiency practices within their own demise.

## Performance

## Investment in water efficiency [GRI EN30 – Partial]

Water efficiency investment	2009	Projected		
		2010	2011	2012
Low*/no cost (£m)	0.15	0.15	0.15	0.15
Water savings (£m)	0.17	0.20	0.20	0.20

\* Investment that are less than £20,000

**Waste**

Reducing total waste produced and the proportion sent to landfill reduces strain on scarce landfill sites and the consumption of virgin materials.

Where we have responsibility for waste management, waste is becoming a significant operational cost in light of annual landfill tax increases. We work actively with our occupiers to improve recycling rates and thereby reduce the service charge portion allocated to waste services.

Reuse and resale of building materials such as plasterboard and aggregates is emerging as a new source of revenue. We are developing a waste management strategy which capitalizes on unlocking value from waste including energy from incineration of commercial waste.

## Savings from waste diversion and revenue from sale of waste [GRI EN30 – Partial]

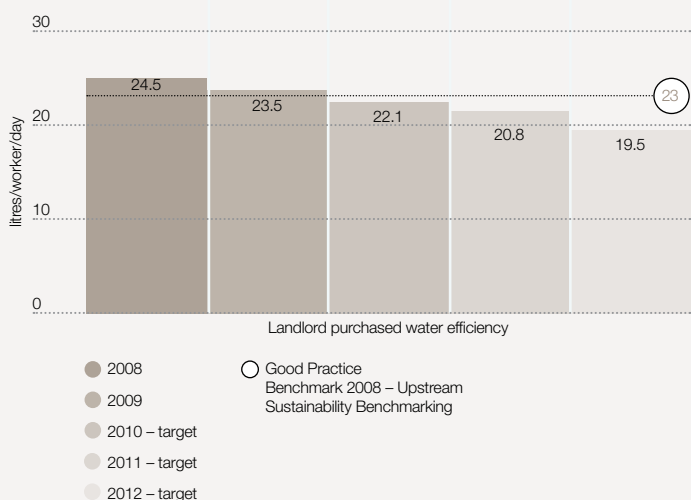
Water efficiency investment	2009	Projected		
		2010	2011	2012
Savings from diversion of waste from landfill (£m)*	0.54	0.70	0.86	0.91
Revenue from sale of waste (£m)**	0.01	0.03	0.05	0.06

\* Projections based on £8 per tonne increase in landfill tax to 2011

\*\* Deriving directly from our assets therefore attributable to us

Whole building (landlord + tenant) water efficiency

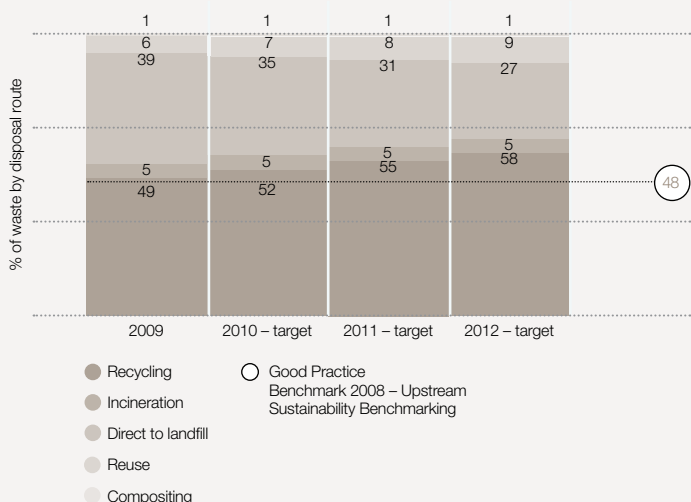
[GRI EN8 – Partial] litres/worker/day



Investment in water efficiency initiatives has a relatively quick payback period (typically less than 1 year). We are therefore witnessing improvements in water efficiency across the portfolio, savings from which are passed on to our occupiers. Water efficiency is improving at a rate of approximately 5% per annum and we are on course to achieve our 2012 target.

Waste disposal route by mass (landlord + tenant)

[GRI EN22 – Partial] % of waste by disposal route



With the corresponding increase in the amount of waste we collect for recycling and Material Recovery Facility (MRF) processing, savings associated with diversion of waste from landfill continue to increase. We are also generating a small, but growing amount of revenue from the sale of waste products which would have ordinarily been sent to landfill, such as plasterboard and cardboard.