

## Business Unit Review – Trillium

Trillium provides Property Partnership services in the outsourcing and Public Private Partnership (PPP) markets. In the six months under review it generated some £61.0m, 18.5% of the Group's underlying operating profit.

This result was a combination of continued good performance from existing contracts and the successful sale of further PPP assets to the Trillium Investment Partners fund for a net consideration of £103.0m. Within our existing contracts, we continued to deliver a strong performance from the DWP contract despite continued high levels of vacation. This surplus space creates an exposure to both the commercial letting market and the residential land market, both of which experienced increasingly challenging conditions in the first half. In the DWP contract and the Royal Mail portfolio this is adversely impacting on profit levels and will continue to do so in the second half.

The PPP market remains relatively robust, as PPP projects continue to be an important part of public sector capital procurement. We are preferred bidder on three projects and actively bidding, by ourselves or in consortia, for a further 15 projects.

The Building Schools for the Future (BSF) programme continues to be an area of opportunity for the Trillium business and closure was reached on the first phase of the Kent BSF on 24 October. It forms part of the overall £1.8bn BSF programme in Kent which plans to rebuild or renew its secondary schools over a period of 10 to 15 years. Approximately £180m will be invested in transforming the first 10 schools. Three of these schools will be delivered through Private Finance Initiative, with Trillium contributing £6m of equity capital.

There continues to be interest in the benefits of PPP for the waste sector, renewed activity in local authority regeneration and an increasing focus on improving the efficiency of the Central Government estate. However, we are experiencing increased delays to the closure of some projects as the current economic conditions, in particular the rising cost of debt, have created some affordability issues.

### Property Partnerships

- DWP

Operating profits rose by £14.3m to £59.2m reflecting £17.7m from one-off items including historic shared savings agreed with DWP. Underlying operating profits were down £3.4m as vacations outweighed the positive impact of indexation and new properties. We have had considerable success in letting and selling surplus properties in the first half, despite a weakening property market. We have disposed of 78,900sq m of space in the period and let a further 29,900sq m. However, the ongoing rate of vacation has meant that the total amount of vacant space has decreased only slightly over the six month period from 208,000sq m to 204,100sq m.

- Norwich Union

Underlying operating profits increased by £1.8m to £6.6m. This performance benefited from completion of the refurbishment of their head office in Norwich in the past year, which increased the revenue received.

- DVLA

With the completion of the main DVLA HQ offices in Swansea, underlying operating profit increased by over £1m to £2.9m as we started to receive a commercial return on the investment we have made into their estate over recent years.

- Royal Mail

The portfolio comprises both a freehold investment portfolio and surplus leasehold space. The investment portfolio is primarily occupied by Royal Mail with the balance let to third parties or vacant. Our main focus is dealing with the surplus leasehold space. With limited occupier demand for these types of large distribution centres during the first half of the year, we have not been able to make significant progress with lettings. As a result, we have charged the income statement with an additional onerous lease provision of £4.3m.

- Accor

Rental income on our portfolio of Accor hotels is based on a fixed percentage of each hotel's turnover. Our operating profit increased by 24% to £14.4m largely reflecting the full ownership of all 29 of the hotels in the half year as compared to the prior half year to September 2007.

### **Trillium Investment Partners**

The initial commitments of £1.136bn made when Trillium Investment Partners was established included £200m headroom for the sale of further assets into the fund up to December 2008. In July 2008 a further 13 assets were sold into the fund for a net consideration of £103.0m, generating a profit of £17.3m. At 30 September we still held 14 assets with a book value of £165.9m for sale in subsequent tranches. We also continue to evaluate opportunities for further acquisitions of PPP projects where these offer cash and return characteristics appropriate for ultimate ownership by Trillium Investment Partners.

## Trillium Financial Results

The results for the period are set out in the table below:

**Table 3: Trillium financial results**

	Six months ended 30 September 2008 £m	Six months ended 30 September 2007 £m	Year ended 31 March 2008 £m
Contract level operating profit / (loss)			
- DWP	59.2	44.9	93.7
- Norwich Union	6.6	4.8	11.1
- Barclays	1.0	0.9	1.9
- DVLA	2.9	1.8	3.7
- Telereal II	6.5	7.6	15.5
- Accor	14.4	11.6	27.1
- Royal Mail	(2.6)	2.1	4.1
- BBC	-	-	9.2
Bid costs	(11.8)	(3.1)	(11.9)
Central costs	(15.2)	(15.1)	(25.3)
Other	-	2.3	-
Underlying operating profit	61.0	57.8	129.1
Net deficit on revaluation of investment properties	(46.0)	(8.8)	(24.9)
Profit on disposal of properties	2.2	15.1	18.1
Goodwill impairment	(147.6)	-	-
<b>Segment (loss) / profit</b>	<b>(130.4)</b>	<b>64.1</b>	<b>122.3</b>
Share of (loss) / profit from Investors in the Community (IIC) (joint venture)	(0.3)	0.1	0.1
Share of loss of Trillium Investment Partners (associate)	(2.0)	-	(0.5)
Profit on sale of interests in Trillium Investment Partners (discontinued operation)	17.3	-	37.5
Impairment of assets held for resale (discontinued operations)	(2.6)	-	-
Profit on sale of Meterfit (discontinued operation)	-	10.0	10.0

## New business

Deteriorating property values coupled with scarcer and more expensive debt are making it harder to complete transactions in our markets. This was the main reason behind the impairment of Trillium's goodwill during the period which is explained in more detail on page 18.

## Property Partnerships

- Defence Training Review

Metrix, our 50:50 joint venture with QinetiQ, remains preferred bidder for this major PPP project to create a 280,000sq m new Defence Training college at St. Athan in South Wales. This project has been faced with a significant cost increase but during October, the Minister of State for the Armed Forces confirmed that considerable progress has been made towards achieving an affordable, value for money solution. He also confirmed the MoD's continuing commitment to the project and the view that, subject to funding issues being satisfactorily resolved, formal MoD approval will be achieved in spring 2009, with financial close in mid 2010.

- Workplace 2010

We are one of two short-listed bidders to provide full property outsourcing to the Northern Ireland Civil Service under a 20 year contract covering over 200,000sq m. Like other PPP projects, this project has faced affordability issues in the current economic climate and this, together with the Authority wishing to have clarity on the ownership of Trillium, has led to the bid process being suspended until early 2009.

## PPP

- Education

Our strategy of becoming a leading player in the BSF programme is now yielding tangible success. As referred to above, we successfully closed the Kent County Council BSF on 24 October, as well as the Inverclyde Schools PPP (in which we have a 25% stake).

We are one of two short-listed bidders for the Birmingham BSF project, where we are working in partnership with RM plc. The first phase covers three schools, with capital value of £80m, with a further seven schools and £120m construction anticipated in the subsequent phase. We have also identified target projects in the next two BSF waves.

- Other

We remain preferred bidder for Norfolk Waste Management Contract A through our partnership with Norfolk Environmental Waste Services and Cyril Sweett. Closure, in common with a number of other PPP projects, has been delayed by affordability issues. Financial close is expected in early 2009.

As part of the GSL Investment Partnership, Trillium remains a member of the preferred bidder consortium for the €470m Thornton Hall Prison PPP project in Ireland. Financial close is expected in the first half of 2009.