

# Primary Health Properties (PHP)

27 August 2008

## 300p

Secure cashflows, in line with expectations

### Share Price: 300p



Source – Digital Look

**12m High:** 393p

**12m Low:** 235p

**Market Cap:** £100.8

**Shares in Issue:** 33.59m fully diluted

**NAV/Share:** 373.4p

**Gearing:** LTV 62%

**Interest Cover:** 2.1x

**EPIC Code:** PHP

**Sector:** Real Estate

**Market:** London Full List

**Joint Brokers:** Numis Securities

KBC Peel Hunt

**PR:** Bell Pottinger Corporate & Financial

**Website:** [www.phpgroup.co.uk](http://www.phpgroup.co.uk)

**Description:** PHP is a UK property company with strong defensive characteristics: it is focused on modern, purpose-built, pre-let premises for GP surgeries and pharmacies and enjoys 18+ year leases and NHS funding of rents.

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PHP delivered interims in line with our expectations. These confirm our view on this property company as being largely protected from market influence thanks to its business model. This is focused on purpose-built premises for GPs, with long-term leases and rent payments funded by the NHS, which results in secure cash flows with good long-term visibility. Key points are:

- The annualised rent roll was up 28.3% on H1 2007 at £18.6m, reflecting the expansion in the property portfolio and the company's effectively upward-only rent reviews.
- Due to lower costs and the absence of performance fees, operating profit before revaluation and financing costs stood at £7m, a high 76.2% of rents and related income.
- Profit after tax adjusted for unrealised losses and one-off costs grew by 23.7% to £2.7m, and the interim dividend was raised by 10% to 8.25p/share.
- NAV per share rose from 369.4p in H2 2007 to 373.4p. This included 14p derived from a higher fair value of interest rates swap in the balance sheet equity account. Before this addition, NAV per share stood at 359.4p. Reported passing yield (rental yield based on past rentals) shifted by 20bps, rising from 5.35% to 5.55%.
- The company has indicated that on a DCF basis, 104p would be added to NAV per share, with the following assumptions (same as MedicX Fund's): 7% discount rate, 3% rent increase, 1% capital gain rise. Interestingly, terminal value represented a modest 25% of this DCF-based valuation which is positive as it implies that the bulk of the valuation is derived from visible cashflows.
- The business is expanding thanks to the ongoing reform of public primary care. PHP added several premises recently, including a large one in May which leverages the drive towards a loose polyclinic model of primary care services.
- Bank covenants are still comfortably met, with LTV at 62% v. 75% maximum allowed and interest cover at 2.1x v. 1.3x minimum required.
- Our forecasts for 2008 are unchanged due to the company's sustained cashflows over the long term, a feature which stands out positively in a market where profits and dividends are being slashed.
- The downturn in the property sector has inevitably affected the stock but it retains its strong defensive characteristics.

Period	Sales	Declared Profit	Adj. Profit	Adj. EPS	P/e Ratio	Dividend	Yield	NAV	Discount
Dec	£m	£m	£m	p	p	p	%	P	%
6/2006A	11.1	18.4	3.9	16.5	18.2	13.5	4.5	421	28.7
6/2007A	14.1	14.3	4.0	14.6	20.5	15.0	5.0	450	33.3
12/2007/A	15.7	-12.8	4.2	13.8	21.7	15.5	5.2	369.4	18.8
12/2008/E	18.0	2.0	4.2	12.5	24.0	16.5	5.5	373.4	19.7

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PHP's H1 2008 Interims

FYE December £m	H1 2007	H1 2008	Var %	H2 2007
<b>Profit &amp; Loss Account</b>				
Annualised delivered rent roll (passing rent, before delivery of all commitments)	14.5	18.6	28.3%	16.2
<b>Rental and related income</b>	<b>7.6</b>	<b>9.2</b>	<b>21.5%</b>	<b>8.1</b>
Administrative expenses, of which	(3.5)	(2.1)	-39.1%	(2.0)
<i>Management incentive fee *</i>	(1.8)	0.0		0.0
<i>REIT conversion charge *</i>	0.0	(0.2)		0.0
Goodwill impairment charge *	(0.1)	(0.1)	-28.6%	(0.1)
Impairment loss *	0.0	0.0		(3.8)
<b>Operating profit before revaluation &amp; financing</b>	<b>4.0</b>	<b>7.0</b>	<b>75.2%</b>	<b>2.3</b>
<i>as a % of rental and related income</i>	<i>52.9%</i>	<i>76.2%</i>	<i>44.2%</i>	<i>28.5%</i>
Net financing costs	(3.7)	(4.4)	18.9%	(3.9)
<b>Operating profit /(loss) before reval. result</b>	<b>0.3</b>	<b>2.6</b>	<b>739.9%</b>	<b>(1.6)</b>
<i>as a % of rental and related income</i>	<i>7.8%</i>	<i>37.4%</i>		<i>ns</i>
Fair value gain /(loss) on derivatives *	0.0	1.6	<i>ns</i>	(2.8)
Revaluation gain /(loss) on properties *	5.1	(4.7)	<i>ns</i>	(13.6)
<b>Reported profit /(loss) before tax</b>	<b>5.4</b>	<b>(0.5)</b>	<i>ns</i>	<b>(18.0)</b>
<b>Tax charge</b>	<b>(0.1)</b>	<b>(0.2)</b>	<b>82.5%</b>	<b>0.0</b>
<b>Reported profit /(loss) after tax</b>	<b>5.3</b>	<b>(0.7)</b>	<i>ns</i>	<b>(18.0)</b>
<b>Adjusted profit before tax</b>	<b>2.3</b>	<b>2.9</b>	<b>26.4%</b>	<b>2.3</b>
<b>Adjusted profit after tax</b>	<b>2.2</b>	<b>2.7</b>	<b>23.7%</b>	<b>2.3</b>
<i>* items excluded from adjusted earnings</i>				
<u>Per share data:</u>				
<i>Average number of shares</i>	27.7	33.6	21.4%	33.6
Earnings (loss) per share p	19.1	(2.0)	<i>ns</i>	(53.7)
Adjusted earnings (loss) per share p	7.9	8.0	1.9%	6.7
Dividend p	7.50	8.25	10.0%	8.25
<b>Balance Sheet Data</b>				
Investment and development properties	279.6	322.9	15.5%	285.3
Total properties owned and leased	282.5	325.8	15.3%	288.3
Commitments, incl.deposits & development loans	38.5	26.9	-30.1%	35.9
Total portfolio (owned, leased and committed)	321.0	352.7	9.9%	324.2
Bank debt, net of cash	132.0	198.7	50.5%	155.3
<i>as a % of investments</i>	<i>47.2%</i>	<i>61.5%</i>	<i>30.3%</i>	<i>54.4%</i>
Gearing debt as % gross assets	47.3%	62.0%	31.1%	56.2%
Interest cover	2.05	2.10	2.2%	2.08
Revaluation surplus/(deficit)	5.1	(4.7)	<i>ns</i>	(13.6)
Net assets	151.1	125.4	-17.0%	124.1
<u>Per share data:</u>				
Shares in issue end of period	33.6	33.6		33.6
NAV per share p	449.8	373.4	-17.0%	369.4

“28.3% increase in annualised rent roll...”

...combined with lower costs”

“Steady growth in adjusted profits”

“Interim dividend raised”

“An expanding portfolio...”

“...whilst LTV and interest cover ratios remain solid”

“Slight rise in NAV per share”

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Management	Major Shareholders														
<p><b>Non executive Chairman:</b> Graeme Elliott</p> <p><b>Managing Director:</b> Harry Hyman</p> <p><b>Property Director:</b> Tim Walker-Arnott</p> <p><b>Property Management:</b> a team of six, based in Woking</p>	<table> <tr> <td>Nexus</td> <td style="text-align: right;">6.34%</td> </tr> <tr> <td>Legal &amp; General Group PLC</td> <td style="text-align: right;">5.15%</td> </tr> <tr> <td>Axa SA</td> <td style="text-align: right;">4.90%</td> </tr> <tr> <td>Newton Investment Management</td> <td style="text-align: right;">3.98%</td> </tr> <tr> <td>Aberdeen Asset Management</td> <td style="text-align: right;">3.62%</td> </tr> <tr> <td>Montanaro Fund Managers Ltd</td> <td style="text-align: right;">3.18%</td> </tr> <tr> <td>UBS Global Asset Management</td> <td style="text-align: right;">3.12%</td> </tr> </table>	Nexus	6.34%	Legal & General Group PLC	5.15%	Axa SA	4.90%	Newton Investment Management	3.98%	Aberdeen Asset Management	3.62%	Montanaro Fund Managers Ltd	3.18%	UBS Global Asset Management	3.12%
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Key Dates	Key Milestones														
<p><b>AGM:</b> June 2008</p> <p><b>Dividend Payment:</b> 20 November 2008</p> <p><b>Next Interim Results:</b> August 2009</p> <p><b>Next Full Year Results:</b> March 2009</p>	<p><b>1994</b> Business model put forward by Harry Hyman</p> <p><b>1995</b> Purchase of a small portfolio and incorporation</p> <p><b>1996</b> Floated on AIM</p> <p><b>1998</b> Full Listing on the London Stock Exchange</p> <p><b>2002</b> Wanless Review regarding the reform of the NHS</p> <p><b>2007</b> Darzi Interim Report launching the reform of public primary care</p> <p><b>2008 (May)</b> Largest acquisition yet: Port Talbot (£15.6m)</p> <p><b>2008 (June)</b> Darzi Review expanding on initial reform</p>														

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