

Phoenix Spree Deutschland

Fund Update
January 2009



PMMPARTNERS

- German economic conditions worsen but housing market remains stable
- Continuing focus on 'bedding in' acquisitions and asset management
- Currency movement creates further benefit for sterling investors
- Loan terms being negotiated for next tranche of acquisitions
- First annual valuation commissioned



Phoenix Spree Deutschland

91%
Occupancy

7.3%
Running yield

€101.9m
assets notarised

107,538
sqm of lettable area

Portfolio Overview

As at the end of December 2008, Phoenix Spree Deutschland had invested, or committed to invest, funds of €101.9m across a total of 81 German properties, representing a gross lettable area of 107,528 sqm and fully occupied yield of 8.1%. The average purchase price per sqm paid for all properties was €948 (€810 when considering just residential properties including outstanding completions).

PSD has completed on €86.5m or 85% of assets based on the total notarised asset pool of €101.9m. Outstanding commitments or notarised assets stand at €15.3m. PMM is in discussion with a number of lenders with a view to agreeing loan terms which would enable it to complete these remaining transactions in H109.

PMM last exchanged on a contract in early September 2008. In the final quarter of 2008 no additional acquisitions were made. PMM does not expect the Fund to make any acquisitions in Q1 2009. Thereafter, any further acquisitions will be subject to market conditions.

Table 1: PSD Portfolio Summary

	Acquisition metrics				Q308		Q408	
	Purchase price (€)	Area sqm	Price € sqm paid	Rent sqm (€)	*Rent sqm (€)	Void rate (%)	Rent sqm (€)	Void rate (%)
PSD Portfolio								
Nursing homes	9,460,000	5,195	1821	11.3	11.3	0%	11.3	0%
Residential	45,694,535	54,085	845	5.7	4.2	6.3%	5.6	8.0%
Office	6,850,000	7,937	863	7.8	7.8	32%	8.1	32%
Commercial/Mixed use	24,534,000	22,128	1109	7.0	4.7	6.7%	7.2	6.7%
Completed portfolio total:	86,538,535	89,345	969	6.5	5.0	8.1%	6.5	9.0%
<i>H109 Outstanding completions</i>	<i>15,384,710</i>	<i>18,192</i>	<i>846</i>	<i>5.7</i>				
PSD Fund Summary:	101,923,245	107,538	948	6.39				

*The Fund completed on a number of buildings in the Q408. The rent per sqm (and corresponding void rate) for the Q308 therefore under-estimates the actual rent per sq/m. On a like for like basis, the rent per sq/m has remained stable at around €6.4 per sq/m.

On its completed portfolio, the Fund has an overall occupancy rate of 91% in the Q408. PSD is actively working with Treureal, the property manager, to reduce vacancies from the current level of 9% down to the long term target of 4%.

Gross underlying arrears are currently €319k. A large proportion of this arrears balance is due to ongoing previous owner reconciliations, relating to recently acquired properties that are still being transitioned to the ownership of the fund, where some tenants are continuing to pay rents to the previous owners bank accounts.

For the first 6 months of ownership there is an inevitable reduction in performance following the handover from the previous owner / property manager. PMM Partners expects arrears and vacancies to improve once the properties have been owned by the Fund for a period of time.

PSD has currently budgeted around €1m of investment expenditure across the portfolio. For such renovation projects, the Fund targets a minimum return of 15% on the investment outlay.

€48m of debt has been drawn down to date and locked in for an average term of seven years giving a current net debt to asset ratio of around 50%. Following the completion of its acquisition programme, the Fund is targeting a cash reserve buffer of at least €4m and a loan to value of no more than 70%.

Residential

PSD's residential portfolio is the largest component of the Fund's total assets, accounting for 60% of total investment. PSD owns or has notated on 1,271 residential units/74,738 sqm, representing €61m of acquisitions. The Fund's four largest residential markets by investment are Hannover (32%), Berlin (22%), Nurnburg/Furth (20%) and Bremen (16%).

The residential vacancy rate is currently running at 8%. Residential arrears are currently €228k. For any acquired building, these two performance metrics typically deteriorate for the 6-12 month period post completion, while tenants, service companies and property managers adjust to the change of ownership. In particular, a large proportion of these arrears relate to service cost and previous owner reconciliations which are in the process of being completed. PMM Partners are working closely with the PSD's property managers to ensure that newly acquired properties are 'bedded in' as quickly as possible with the vacancies and arrears being managed downwards and brought into line with the Fund's long term targets.

Table 2: PSD investment by city

City	€m	%	sq/m
Berlin	29.3	28.7%	27,875
Bremen Nursing Homes	9.5	9.3%	5,195
Bremen	8.6	8.5%	9,903
Dinslaken	2.0	2.0%	1,680
Egelsbach	1.9	1.9%	1643
Fürth	5.5	5.4%	7,882
Hamburg	0.8	0.8%	702
Hanau	1.3	1.3%	1174
Hannover	19.4	19.0%	21,977
Holzgerlingen	5.4	5.3%	5,258
Nürnberg	10.4	10.2%	15,294
Pforzheim	4.1	4.0%	3657
Rendsburg	2,7	2.6%	3847
Verden	1,0	1.1%	1449
Total	101.9	100%	107,538

Table 3: PSD 10 Largest Tenants

Asset	Tenant	Rent per annum €	% of total
Nursing Homes	Senioren Wohnpark	702k	9.39%
Zerrennerstraße	Merkur-Spielothek	168k	2.25%
Max Eyth Straße	Werbas AG	163k	2.18%
Hünxnerstraße	Edeka	144k	1.93%
Max Eyth Straße	Solution-GmbH	120k	1.60%
Argentinische Allee	Medycur GmbH	73k	0.98%
Albertinenstraße	Interkult. Initiative	57k	0.76%
Ritterstrasse	Reha-Zentrum	56k	0.75%
Max Eyth Straße	Curetis AG	54k	0.72%
Total		€1.53m	20%

Table 4: PSD Residential Operating Metrics

City/Region	Acquisition metrics			Q308		Q408	
	Purchase price (€)	Area sqm	Price sqm paid (€)	Rent/sqm (€)*	Void rate (%)	Rent/sqm (€)	Void rate (%)
Berlin	12,440,000	14,292	870	4.0	8.3%	5.3	10.6%
Bremen	9,086,046	10,562	860	5.2	5.5%	6.0	6.0%
Hannover	8,528,000	9364	911	2.2	6.7%	5.9	10.7%
Rhine-Main	3,265,000	2816	1,159	6.0	6.3%	7.2	1.3%
Nürnberg/Fürth	12,375,488	17051	726	4.5	4.8%	5.1	6.9%
Total	45,694,535	54,085	845	4.2	6.3%	5.6	8.0%

In 2009, PMM will shift its focus from ‘bedding in’ its acquired assets to enhancing the Fund’s running performance. Measures will include driving rent inflation, yield-positive refurbishment projects with a minimum return on investment of 15% and improvements to the tenant profile and structure. PSD is targeting rent inflation of between 2-3% per annum across its residential property portfolio.

Nursing Homes

Germany has one of the most rapidly maturing population demographics in Europe. Now in its advanced stage, the country is experiencing increasing levels of life expectancy, lower birth rates and an ageing population.

Given these structural trends, the Fund acquired two new build Nursing Homes in the north of Bremen. The aggregate purchase price paid for both homes was €9.4m, which represented a running yield of 7.4%. The homes have been let on a 20 year triple net, fully repairing lease with two further five year options. The tenant, Senioren Wohnpark Weser, is an established regional operator with significant scale and industry experience.

PMM Partners believe that these investments in a demographically and structurally sound market offer a stable and cash generative investment. The nursing homes account for 9% of the Fund’s rental income and currently carry no debt.

Office

The Fund has acquired two office buildings for €6.85m or around 7% of PSD’s total investment. Both are ‘value add’ properties, where vacancies can be reduced and the rental structure of the property improved. They were acquired on high yields, for considerably less than the cost of construction. Stripping out units which require refurbishment, the underlying vacancy rate is currently running at 21%.

Occupancy at Max Eyth Strasse in Holzgerlingen is expected to improve in Q109, increasing from 65% in the Q408 to 68%. This uplift will reflect the recent successful negotiation of a number of new lease agreements. Net rental income is expected to stand at €433k per annum once these new agreements are in place. The current running yield is 6.7%. It is intended that the vacancy rate can be brought down to below 10% by the year end, giving a running yield of around 9%.

The Fund has commissioned an architect to advise on the refurbishment of its second office building at Willy Brandt Platz in Nürnberg. The building was acquired in March 2008 for €1.45m/€541 per sqm and has around 520 sqm or 24% of vacant lettable space. The low price paid reflected the need for renovation investment. This will be focussed on renewing or refurbishing the façade, the construction of a new entrance foyer and redecoration of rental space. PMM Partners expect this renovation programme to complete in Q409. Given the building’s excellent location and proximity to the main train station, PMM believes that vacant space should be let at favourable rents and produce a sustainable running yield of 9% to 10%.

Table 5: PSD Office Operating Metrics

City/Region	Acquisition metrics				Q308		Q408	
	Purchase price (€)	Area sqm	Price € sqm paid	Rent sqm (€)	Rent sqm (€)	Void rate %	Rent sqm (€)	Void rate %
Max Eyth Strasse Holzgerlingen	5,400,000	5,258	1,027	9.5	9.3	35%	9.3	35%
Willy Brandt Platz Nürnberg	1,450,000	2,679	541	5.7	4.3	24%	4.3	24%
Total	6,850,000	7,937	863	7.8	7.8	32%	8.1	32%

Mixed Use & Retail

The Fund has continued to make good operational progress on its portfolio of 11 mixed use and retail buildings, reflecting a number of new tenancy agreements being signed. Most notably, 498 sqm of vacant space was let in Q408 at Otto Suhr Allee in Berlin for an average rent of €7 per sqm, the building is now 96% occupied compared to 79% on acquisition.

Table 6: PSD Mixed Use & Retail Operating Metrics

Property	Acquisition metrics			Q308		Q408	
	Purchase price (€)	Area sqm	Price sqm paid	*Rent sqm (€)	*Void rate %	Rent sqm (€)	Void rate %
Total	24,534,000	22,128	1,109	4.7	6.7%	7.2	6.7%

PSD has recently received a payment of €70k from the vendor of Argentinische Allee, a classical villa in Berlin-Zehlendorf which the Fund completed on at the end of October 2008. This payment arose as the rents on completion were around 12% lower than guaranteed by the vendor in the purchase contract. This was due to a residential tenant who occupied around 120 sqm terminating his lease contract after contracts were exchanged. PSD are currently in negotiations with a potential tenant to fill this space.

In our September 2008 update, we discussed the building at Huxnerstrasse in Dinslaken which was affected by local mining activity. After successful negotiations, the mining company have accepted responsibility and required associated repairs and have agreed to pay for the works at a cost of around €250k.

Potential Sale of Property

As reported in the last update, PMM has been approached by a developer wanting to acquire one of the Fund's properties located in the centre of Fürth. The developer is constructing a new shopping centre and the property forms part of the proposed scheme. PMM Partners have now agreed terms which will give the developer a one year option to acquire the property at a significant premium to the price paid by the Fund in 2007. In return for granting the option the Fund will receive a reservation fee. The contract is expected to be signed within the next month and further details will be provided in the next update.

Borrowing and liquidity

The Fund has drawn down loans representing €48.3m as at the end of December 2008. Based on acquisition prices, this represents a loan to value of 55.8% and a blended interest rate of 5.3%, which has been fixed for a period of 7 years. The fund currently has around €5m of cash which when taken into account results in net debt of c.€43m and gearing of 50%.

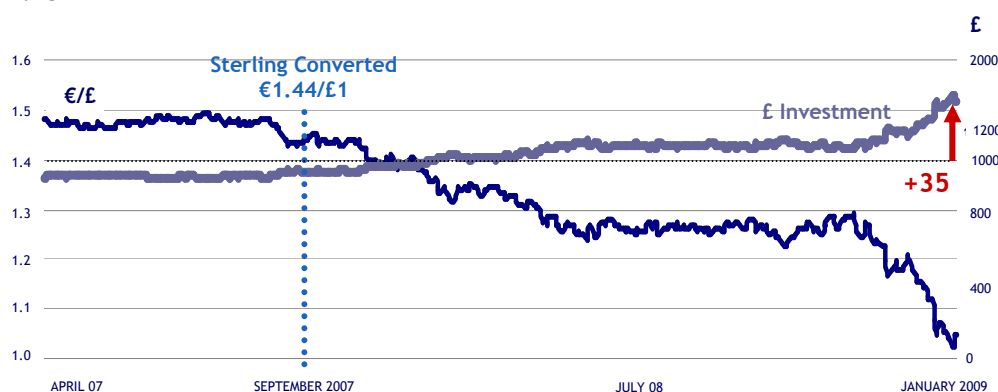
The conditions in the credit market deteriorated sharply in October following the collapse of Lehman and the resulting near failure of Hypo Real bank in Germany. As a result of the effective closure of the lending market, the Fund deferred completion on a number of transactions until the first half of 2009. In total, outstanding transactions which require financing represent €15.4m. In December 2008, a number of banks have shown an interest in recommencing lending. PMM are currently in late stage negotiations with two such institutions and the aim is for PSD to have financing in place to complete its outstanding commitments by the end of the Q209. Effective long term borrowing rates have remained broadly flat in the last six months, as rises in credit margins have been offset by a reduction in swap rates. Assuming current conditions remain unchanged, this tranche of debt is expected to be secured at a rate of around 5.5%. Importantly, all the properties that require finance are located in one special purpose vehicle, which ring fences the liability and protects the Fund in the unlikely event that it is unable to meet its purchasing commitments.

Currency Exposure & Valuation

Currency movements have had a considerable and positive impact on the investment performance of the fund. Recent volatility in the foreign exchange markets has meant that Sterling has sharply devalued against the Euro.

Sterling denominated investments into Phoenix Spree Deutschland were converted by the Fund into Euro's in October 2007 at a blended exchange rate of €1.44/£1. Given the current €/£ exchange rate of €1.07/£1, a typical £1,000 investment would now be worth around £1,346 or a 35% uplift based independently on currency movements alone*.

**Chart 1: Progression of Euro/Sterling exchange rate:
Currency gains of a £1,000 investment**



*35% investment uplift based on €/£ exchange rate movements only—€1.07/£1 as at 27 January 2009 versus PSD conversion rate of €1.438/£1 in October 2007.

In August 2008, PMM Partners instructed DTZ to carry out an indicative desktop valuation of the funds notarised assets. DTZ reported a figure of €98.9m based on an aggregate notarised purchase price at the time of €88.5m. PMM believe that this uplift reflected the Fund's selective acquisition strategy as well as a relatively stable market in Germany. This indicative desktop valuation suggests 11% uplift in NAV, after acquisition costs and the €/£ rate as at September 2008 (€1.24/£1).

PSD is about to commence its first annual valuation of its assets, the results of which are expected to be made available to investors, along with a formal NAV calculation, in Q2 2009.

Market Overview

After initially sidestepping many of the issues that have impacted the US and UK economic and financial systems, Germany too became victim of the global financial crisis. Q408 saw the bailout of two of its largest financial institutions, Hypo Real and Commerzbank, by the German state.

These financial shocks led to the effective closure of the Pfandbrief market (the market used by bank for refinancing German mortgage debt), creating liquidity issues for most market participants. The availability, rather than the cost of debt remains the key issue and as a result transaction volumes have since declined significantly towards the end of 2008.

Listed European property companies equities have been hit hard - the FTSE EPRA/Europe index is trading 51% lower than at the peak in June 2007, and a basket of popular German real estate stocks are trading at discounts of between 51% and 95% to their Net Asset Values.

PMM Partners believe that, although in many respects the economic slowdown will deepen, the German economy, and property market in particular, should remain relatively resilient, especially when compared to the other Western European economies such as Ireland, Spain and the United Kingdom. Unlike in these countries, Germany has low homeownership (e.g. 43% vs. 70% in the UK) and a cultural aversion to debt. As a result, there has been no housing or consumer 'debt fuelled' bubble and at the starting point of this crisis, the federal budget was balanced.

PMM believe that German residential property is unlikely to experience a significant negative impact due to this slowdown. Rent levels in Germany are amongst the lowest in Western Europe, which makes housing relatively affordable. Moreover there has been little inflation in rents in the last decade, while construction of new homes is at the lowest level since the Berlin Wall fell in 1989. In most German cities, prices for residential buildings have seen a modest adjustment over the last six months, with asking prices being reduced by up to 5%. In Berlin, the high prevalence of international buyers caused prices to rise significantly in 2006 and 2007, meaning they have more recent gains to give up, and as such have seen a reduction of between 10% to 15% since reaching a peak in the summer of 2007.

German commercial property is more likely to be impacted, with demand falling faster than output, resulting in downward pressure on rents and a fall in the value of commercial real estate assets. Most impacted are likely to be those assets which were acquired by leveraged international buyers, such as supermarkets and A class office properties. PMM believes that the prices for these assets have already fallen by up to 20%, since the peak in mid 2007.

PMM expects property companies with large exposure to the commercial sector, near term refinancing risk or those that are highly leveraged to struggle most in 2009. PMM Partners are happy to confirm that PSD does not fall into any of these categories.

The next PSD Fund Update is due in April 2009.

Phoenix Spree Deutschland

Fund Fact Sheet
January 2009

Investment Objective

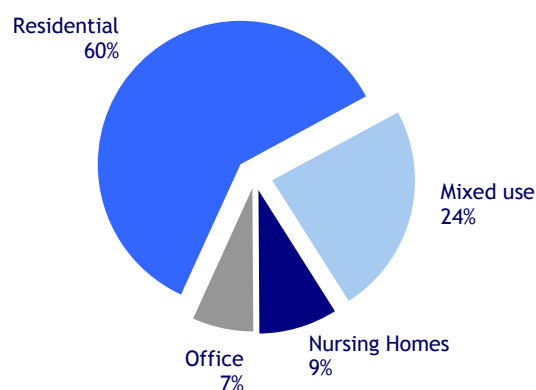
The Fund's investment objective is to focus on acquiring and actively managing, high quality pre-let properties in Germany. Buildings will mainly be bought individually or in small packages. The Fund is targeting an initial gross yield of 7.4%. The majority of the Fund's investments will be made in the residential market, supplemented with selective commercial properties. Non recourse loans will represent up to 75% of the purchase price.

Fund Metrics

Initial net equity:	€53m
Target assets under management:	€125m
Notarised contract value:	€101.9m
Running yield:	7.3%
Fully occupied yield:	8.3%

Investment Returns	Assets	Valuation	NAV +/-	NAV ²
Q3/08 Indicative Valuation	€88.5m	€98.9m	+ 11p	111p

Allocation by Segment



Key Operating Metrics

	Q3 08	Q4 08	Difference
Value of notarised assets	€101.9m	€101.9m	-
Value of completed assets	€84.4m	€86.5m	+€2.1m
Residential units notarised	1,105	1,105	-
Commercial units notarised	166	166	-
Sqm notarised	107,538	107,538	-
Value of loans drawn down		€48.3m	
Loan to value		55.8%	
Vacancy rate	9.8%	9.0%	-0.8%
Rental arrears balance ¹	€139k	€319k	+€180k
Purchase price per sqm ²	€809	€809	-
Purchase price per residential unit ²	€55,159	€55,159	-

¹ Given the number of buildings completed in the Q408, a large component of the increase in total arrears is due to previous property manager reconciliations which are outstanding. PMM Partners expects this metric to stabilise once the reconciliation process has been completed.

² Indicative, first valuation expected in Q209

Investment by City	€m	%	sq/m
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Fund Advisor

The Fund is advised by PMM Partners, an which was formed to address opportunities in the real estate market. PMM Partners has advised on over 150 real estate transactions since 2005, valued at more than €200 million. Through analytical, research-driven processes and direct deal experience the property advisory team have greater insights into the strategies and disciplines of the Funds they advise on.

www.pmm-partners.co.uk

Phoenix Spree Deutschland Limited

Launch:	April 2007
Close:	July 2007
Listing:	CISX (Jersey)
Lifespan:	3-8 years (maximum 10)



Phoenix Spree Deutschland

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