



CITY INSIGHTS

CareCapital Group Plc (AIM: CARE)

AIM: Real Estate Recent Price: 35.75p Market Cap. £35.75m

Investor and developer of healthcare properties

CareCapital is a developer and investor in primary healthcare real estate in the UK and Germany. Originally founded in 1994 to advise groups of doctors on premises development, the Company had, by the mid-1990s, moved into direct long term investment in medical properties. It was admitted to AIM in August 2006. As at the 31st March, the Company had a property portfolio of twenty-two medical centres and other buildings, valued on yield at £35.3m, and a further nine developments in progress scheduled for completion before end 2009. There is also a pipeline of nineteen projects in the UK and others in Germany.

...with a healthy project pipeline

Shift of resources to the local primary sector

The primary healthcare sector is growing rapidly across Europe as governments move services from hospitals to a local level. This reflects the budget pressures that health authorities face, particularly at the secondary level where hospital treatment costs have consumed large proportions of the total budget. Faced with the responsibility of allocating scarce resources, governments are seeking to alleviate cost pressures by establishing multi-purpose healthcare facilities in the local communities.

Properties valued on yield at £25.5m net of borrowing

In the UK, where a substantial proportion of doctors' surgeries, and other NHS facilities operated by the Primary Healthcare Trusts (PCTs), are now considered undersized or otherwise unfit for purpose, CareCapital has focused on investing in larger, 'new build' premises providing a range of services. The current rent roll on existing properties is £1.94m with a valuation on yield and net of debt of £13.9m at 31st March (£8.6m at the date of the IPO). For the nine UK developments in progress, prospective rents are £2.4m and the valuation on yield, net of debt, is £10.5m.

Profits achieved in 2006

In its final results for the year ended 31 December 2006, CareCapital made a pre-tax profit of £1.7m after charging just under £590,000 in costs associated with the AIM listing (2005: loss of 295,000). Under IFRS, adopted for the first time, revaluation surpluses of £3.5m were included in profits. The Company's net assets were £13.4m, 17.4p per share. CareCapital's consolidated net debt at the year end was £16.6m.

Year end 31 Dec (Figs in £000)	Turnover	EBITA	Pre-tax Profit/(Loss)	(Loss)/ EPS (p)	PE (x)	Div (p)
2005	1,747.6	321.7	(295.4)	(0.5)	-	-
2006	1,832.0	(603.8)	2,297.3	1.7	21.0	-
2007E*	1,990.0	835.0	1,005.0	0.7	51.1	-
2008E*	3,455.0	2,691.0	4,312.0	4.2	8.5	-
Net Assets		£13.38m	Net Debt			£16.55m
Shares in issue		76.75m	Adjusted diluted NAV			21.3p
Fig's under IFRS & restated for 2005; *Forecasts by housebroker, Daniel Stewart & Co						

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CITY INSIGHTS LIMITED
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Origins and Introduction

Company founded in 1994, reconstituted in 2004; reorganised and admitted to AIM in Aug 2006

CareCapital Limited (CCL), the Group's predecessor, was reconstituted in 2004 by the acquisition/amalgamation of the healthcare property interests of Sinclair Montrose Trust with the introduction of £10m of capital - £7.5m from Luxembourg-based private equity company, Asgard Real Estate and a further loan of £2.5m from venture capital firm, Valhalla Partners (both managed by AXA REIM).



On 31st July 2006, a reorganisation of the capital structure was undertaken in anticipation of Admission to AIM, which was achieved in early August 2006. Daniel Stewart & Co. managed a new issue of share capital on 31 July - 706.96m shares, 0.1p nominal, and then consolidated on the basis of 1 new ordinary at 1p for every 10 of the former. Total funds raised from the market net of expenses was £1.46m via two transactions; first, an issue of new ordinary shares was made at 0.10p at par, and secondly, a placing of 5m new ordinary shares at 1p. The original Valhalla loan of £2.86m (including accrued interest) was repaid.

On the 3rd May 2007, Asgard Real Estate disposed of all its shares and no longer has any interest in the Company. A separate announcement on the same date confirmed the placing of 5m shares on behalf of the Sinclair Montrose Trust (in which the Chairman's and the Chief Executive's stakes are included) resulting in SMTs holding reducing from 26.2m (34.12%) to 21.2m (27.61%). Total shares in issue are 76.75m.

£29.5m property portfolio...

By the end of December 2006, the Group had built a property portfolio comprising twenty-one healthcare properties with a gross valuation of £29.5m (2005: £21.4m) provided by Colliers CRE on a yield basis at 5.5%. The current UK property portfolio comprises thirteen medical centres, five pharmacies, two dental practices and a health promotion unit. These properties are spread across the UK.

...and nine more in the UK with a gross value over £51m

In addition, CareCapital has nine new properties under development in the UK, with four of these expected to reach development by the end of 2008 having a gross developed value of £14m. A further five projects with a gross value of £37.2m are scheduled for completion before the end of 2009. The total figure of £51.2m is inclusive of anticipated receipts from the sale of developed properties not required for long term investment (estimated £15.1m).

...while Germany is now seen as a new growth area

In addition, in December 2006, CareCapital made an initial investment of €9.2 m in a healthcare centre in Berlin. This has 34 medical tenants including GPs, specialists, dentists, a dental laboratory, a pharmacy, opticians and a diagnostic centre. This is part of a planned programme of acquisitions in Germany, and a further investment of €4.2m was made in March 2007. These investments are being funded by a major German bank supplemented by CareCapital's own resources.

With further identified development opportunities, the Group will make planned investments totalling EUR 35m (£23.5m) in Germany. Future growth outside the UK is expected to match that within. Details of the individual properties are given later.

Ten projects add over £12m to the NAV

In summary, therefore, the ten projects under development, with an attributable annual rent of £4.6m, should add an estimated developed value of £41.6m. After the deduction of the debt attached to each, the Group's NAV should increase by £12.2m.

Healthcare real estate is extensive...

The Group's core business is investment in and development of healthcare real estate. It acquires, develops and leases property to the healthcare sector which generates income and capital growth. The types of properties that the Group seeks to develop are new build multi-purpose medical centres and polyclinics, incorporating independent sector clinics, dental surgeries, pharmacies and other community facilities. Some larger properties may incorporate more than one unit, and others extended to accommodate additional facilities.

...but a large proportion is considered unfit for purpose

CareCapital recognises that a large proportion of existing properties used by the NHS at the primary health level are either undersized or otherwise not fit for purpose and require extensive upgrading. In addition, Government policy in both the UK and in other European countries is placing increasing emphasis on primary care within the community as being a more cost effective, timely and appropriate provision alongside the secondary level of hospital care. Intermediate Care Facilities and the new category of ISTCs (Independent Sector Treatment Centres) are now operating alongside NHS hospitals and providing additional capacity.

...and primary healthcare alleviates budgetary pressures

While NHS funding is perceived as a long term problem, the Government is seeking to alleviate the budgetary pressures by facilitating and channelling more healthcare provision into the primary sector, thus taking patients away from the hospitals. Although the UK's 'one buyer' system for healthcare is unique, similar developments at the primary level are occurring widely in Europe. This approach is now well established in North America.

This report covers CareCapital's final results for the year ended 31st December, the property portfolio, developments within the healthcare sector, the management team and finally the prospects.

Financial Highlights

First profits achieved...

The results have been prepared for the first time under IFRS and therefore, for comparative purposes, 2005 figures have been restated. The main impact of this is the inclusion in the income statement, rather than in reserves, of the surplus/deficit on revaluation of investment properties. CareCapital achieved its first pre-tax profit of £1.7m (2005: loss of £295,000) as shown below.

...which included revaluation surpluses under IFRS

The increase in top line revenues, 4.8%, was driven by a 12% rise in Group rental income to £1.34m (2005: £1.2m). The increased scale of the business necessitated a 74% increase in administrative expenses to £2.35m, this figure including £589,574 in connection with the AIM listing. The revaluation of the property portfolio resulted in a £3.5m surplus compared with £281,000 in the previous year. CareCapital points out that with several properties coming on-stream each year, and others receiving rent reviews, annual revaluation surpluses on various properties can reasonably be expected on a continuing basis.

Results for the year to 31 December 2006			
	2005	2006	Change %
Revenues	1,747,651	1,832,013	4.8
Cost of sales	(72,719)	(83,560)	
Gross profit	1,674,932	1,748,453	4.4
Administrative expenses	(1,353,167)	(2,352,192)	73.8
	321,765	(603,739)	-
Other operating income	-	251,418	-
Net surplus on property reval's	281,165	3,528,023	-
Operating profit before except's	602,930	3,175,702	426.7
Exceptional costs of AIM listing	0	(589,574)	-
Interest income	244,545	186,608	(23.7)
Interest costs	(1,155,424)	(1,094,027)	(5.3)
Change in fair value of fin. instrum'ts	12,528	29,081	132.1
Profit/(loss) before tax	(295,421)	1,707,790	-
Tax	(88,108)	(1,029,967)	
Profit/(loss) attrib. to equity holders	(383,529)	677,823	-
EPS/(loss) per share basic	(0.54)p	0.93p	-
Weighted average no. of shares	70,696	73,544	-

Interest charges well covered by a guaranteed rental stream...

The level of interest charges reflects that the business is largely financed by debt. Healthcare properties have excellent covenants since the rent payments are paid by Government (the NHS) with no default risk, and have a very low void rate. CareCapital's total debt on the balance includes long term borrowings, including finance leases, of £18.5m and short term borrowings, also including finance leases, of nearly £366,000. Against total debt of £18.9m, the Group has cash and financial instruments of £2.5m, thus £16.6m of net debt compared with shareholders' funds of £13.4m. Gearing is largely irrelevant as the interest charges are more than covered by the guaranteed rental stream.

...though nominal rates are still relatively high

The long term borrowings are secured on the property assets, and are provided by a panel of banks and financial institutions on a project by project basis. Interest charges on the older loans are relatively high since a significant proportion of the debt was agreed in periods of higher rates (6.5% and above), apart from the more recent Euro-denominated debt raised for the German properties which is at 4.5%. There is an opportunity to renegotiate rate charges at a more favourable level.

Cash flow highlights

Operating cash flow deficit...

Cash from operations showed a deficit of £570,615 compared with a surplus of £296,474 last time. This was after taking account of positive working capital adjustments, of £218,915. The deficit reflects the relative immaturity of the business, particularly the high level of overheads compared with rental income.

...with a £6m investment spend on properties

The main feature in the cash flow statement was the total investment of £6.06m on the acquisition of properties. All other capital expenditures on development properties, amounting to nearly £482,000 last year, were construction related. Additional expenditure of £14,293 was incurred on plant and equipment, in reality the purchase of items such as office equipment, computers, etc. The cash outflow before financing emerged at just over £8m compared with only £1.15m in 2005 as the pace of CareCapital's development accelerated. The Company raised £1.46 net new money from a share placing following the Group's AIM listing in August, but also repaid an investors' loan of £2.86m (including accrued interest).

Cash flow			
Year ended 31 December	2005	2006	Change
Profit or loss after tax	(383,529)	677,823	1,061,352
Adjustments:			
Taxation	88,108	1,029,967	
Unrealised net revaluation gains	(281,165)	(3,528,023)	
Other	957,450	957,437	
Depreciation	33,916	33,005	
Write-off of development properties	-	40,261	
Working capital adjustments	(118,306)	218,915	
Cash from operations	296,474	(570,615)	(867,089)
Net Interest	(771,523)	(907,419)	
Purchase of investment properties	-	(6,058,524)	
Capital expen. on devel properties	(651,504)	(481,960)	
Capital expen. on plant and equip.	(28,280)	(14,293)	
Cash flow before financing	(1,154,833)	(8,032,811)	(6,877,978)
Financing:			
Proceeds from share issues	-	1,458,083	
Cash flow in period	(1,154,833)	(6,574,728)	(5,419,895)
(Incr.)/decr. in debt in period	(178,146)	(1,941,533)	
Other movements		(655,410)	
Net debt at start of period	(6,050,497)	(7,383,476)	
Net (debt)/cash at end	(7,383,476)	(16,555,147)	(8,964,890)

Property assets in excess of £29m

On the balance sheet, there are owned assets including investment property assets of £29.5m at 31st December (£21.4m last year) and just over £0.5m on development properties (£64,000 in 2005). In addition, £1.75m of intangible assets represents the goodwill arising on the acquisition of subsidiaries by CareCapital Ltd, the Group's predecessor, on 31 August 2004 when that organisation was reconstituted. Property assets held for investment are initially held at cost, inclusive of capitalised interest, direct attributable cost plus a margin for the recovery of attributable internal overheads. They are then revalued by external property valuers at the balance sheet date.

CareCapital Group Business Model

<i>Bidding may be with a partner and outside UK</i>	CareCapital acquires land and builds or develops a property for subsequent letting to healthcare providers. Development opportunities arise through recommendation and referral or through a competitive bidding process following invitations to tender for developments advertised by the Primary Health Care Trusts (PCTs). For large scale projects, which may have a contract term in excess of twenty years, CareCapital may elect to partner another organisation both in the bidding for the project and in its subsequent development.
<i>Different and protracted time scales</i>	The formalisation of development contracts, after a successful bid, may still take a long time. The possibility of a protracted timescale is factored into the model. Unlike other companies in the sector, CareCapital prefers to retain the freehold rights in its properties. Apart from the generation of a steady income stream, it thus retains not only the opportunity to benefit from any long term capital gain but also, and with the long term in mind, it demonstrates an ongoing commitment to the sector and thus encourages good relationships both with the tenants directly and the PCT.
<i>Good relationships assist the chances of winning bids</i>	CareCapital also desires to offer a 'one stop shop' comprehensive property service, through its contacts with construction firms, clinical and facilities management companies, healthcare planners and clinical staff recruitment agencies. Income from management of facilities is thus additional to a secure rental income. Good relationships are of substantial value in enabling CapitalCare to bid successfully for projects and, having substantial expertise and experience, management boasts a good track record in this field.
<i>CareCapital operates within property market parameters</i> ...	The Group operates within the parameters set by commercial property yields as these may be affected by movements in the wider property market, such as the demand and supply of suitable properties. In fact, because of the healthcare covenants, the yield is likely to be lower than for other good quality commercial properties. Income is expected to increase in the longer term through the rent review process in which the District Valuation Officer must be involved. CareCapital seeks to ensure that income from new lets is adequate to cover not only the interest costs on its mortgage debt, but also provide some carry-over to finance other developments, thus minimising recourse to the market for funds.
<i>...and yields have compressed</i>	The desirability of these low-risk healthcare property assets is reflected in the compression of yields. In their valuation of Group properties, in July 2006, Colliers used a yield of 5.5% to the UK rent roll of £1.3m arriving at a valuation of £23.6m before deduction of £13.5m of debt. Rents from the two German properties now owned are EUR 0.96m (£0.65m), and the valuation on the same yield is EUR 17.3m (£11.74m) before deduction of £7.96m of debt. These valuations appear conservative. In the UK, the general market yield has declined to 4.25% for low risk commercial properties under pressure of demand, and thus the scope for a substantial revaluation of the CareCapital properties, all other things being equal, is a substantial £9m.

The property portfolio

The UK portfolio includes thirteen medical centres, five pharmacies, two dental practices, and one health promotion unit. All except one of these, at Mold, are 100% owned.

<i>Location</i>	<i>Size m²</i>	<i>Description</i>
Burnley, Yorks	777	Prestige Works Medical Centre, in a brownfield regeneration site, comprises a Surgery for seven GPs. This project was developed in collaboration with Sainsbury and completed in 2003.
Clifton, Co Durham	805	Clifton Court is a multi-client medical facility including a six GP Medical Centre with attached Pharmacy. Completed in 2002.
Consett, Co Durham	888+93	Consett Medical Centre, in an area of regeneration, is a multi-occupational site including a nine GP Surgery and an independent Pharmacy. It incorporates additional facilities for minor surgery, therapy, health promotion, training and community services. Completed in 1999 and extended in 2004.
Chafford Hundred, Essex	580	Chafford Hundred Medical Centre, in a new town, is a multi-client facility incorporating a five GP Surgery and dental unit. Completed 1999.
Chalford, Glos	351	Frithwood Medical Centre, in a new town setting, with a four GP Surgery in a retail development including a Tesco Metro, café and betting shop. Completed in 1996.
Hinckley, Leics	675	Station View Medical Centre, on a brownfield site, is a multi-occupational facility, including six GP Surgery and Pharmacy. Completed in 2002 and extended in 2005. Further expansion plans for 2007.
Hornchurch, Essex	764+102	Maylands Health Centre, on reclaimed brownfield land, incorporates a seven GP Surgery and dental unit. Completed in 1997.
Kesgrave, Suffolk	441	The Birches Medical Centre is a four GP Surgery set in a medical campus and includes a day care centre, Early Years nursery and scout meeting hut. The unit was developed in association with Tesco; Care Capital is a partner in a joint venture to progress the scheme.
Leamington Spa	650 + 550	Waterside Medical Centre combines a five GP Surgery, Pharmacy, Health Promotion Unit and Drug Rehabilitation Centre. Main block completed in 2005, additions in 2005.
Lydney, Glos	408	Severbank Medical Centre is a three GP surgery which forms part of a major housing development. It is CareCapital's policy to sell residential and retail components. Completed in 2002.
Restalrig, Edinburgh		Restalrig Park Medical Centre is a five GP surgery in a new town in the outskirts of Edinburgh.
Watlington, Norfolk	396	Watlington Medical Centre, on reclaimed land, comprises a three GP Surgery and forms part of a housing development completed 2003.
Wingate, Co Durham	400 +40	Caradoc Medical Centre, in an area of high deprivation, comprises a three GP Surgery and independent Pharmacy. Completed in 1999.
Adlershof, Berlin	4,100	Adlershof 1 Health Centre is a multi client facility accommodating thirty-four medical tenants. The centre also houses a Radiography unit, dental lab and pharmacy. Completed in 2005.
Konigs Wusterausen	2,652	Medical centre to accommodate 25 GPs. Completed in March 2007.

As illustrations of CareCapital's property assets, the one shown below is of an existing property in Consett with a typically expansive (981 sq. m after extension) modern layout situated in area of regeneration.



New German ventures

German ventures offer better yields with no increase in risk...

The German market is ahead of the UK in community-based healthcare and the quality of the existing buildings with similar covenant profiles is generally superior. These factors, coupled with the development opportunities arising from CareCapital's relationships with the banks and some building contractors, enable it to make investments on rather better yields than are currently available in the UK yields with no increase in risks. The Company's first acquisition in Berlin last December was a 4,100 sq. m (NIA) medical centre in the Adlershof science and technology park in east Berlin (pictured below). The building, housing 34 medical tenants (specialists, dentists and an optician) cost €9.2m (£6.3m) and has an estimated value of EUR 11m (£7.42m). The complex, completed in 2005, also houses a radiography unit, dental laboratory and a pharmacy.



...and more acquisitions will be made

The second property in Konigs Wusterhusen to the south-east of the City - cost EUR 4.2m (£2.8m) and has an estimated value of EUR 6.25m (£4.25m) on a net rental yield as high as 7.9%. This medical centre occupies 2,850 sq. m and provides accommodation for 25 medical tenants, including consultants, an orthopedic rehabilitation unit, a pharmacy and some healthcare related retailers. This acquisition includes an adjoining development site, acquired at a nominal cost, on which the development of an additional 1,000 sq. m medical facility is to be commenced immediately.

UK developments in the pipeline - costs, rents and values

For illustration, the table overleaf provides the financial details of the UK developments under construction, including cost, projected rents and estimated value at completion.

CareCapital - Developments under construction and in the pipeline							
Location	Cap. Cost (Est.)	Projected rents	Devel. Margin	Proj'ct'd Cap. receipts	Mkt value on yield (Est)	NAV on completion	Target completion date
UK							
Bishop Stortford	£3.6m	£234,765	£319,000	£0.38m	£4.3m	£1.0m	Nov '08
Buckley	£11.0m	£823,100	£350,500	-	£7.5m	£2.5m	Apr '09
Coventry	£3.1m	£143,748	£186,000	£1.15m	£2.6m	£0.6m	May '08
Epsom	£7.5m	£186,893	£669,000	£5.0m	£3.4m	£0.9m	Apr '09
Folkestone	£3.5m	£272,000	£100,600	-	£4.9m	£2.1m	Nov '07
Radlett	£2.3m	£154,586	£149,500	-	£2.8m	£0.8m	Jan '09
South Oxhey	£2.2m	£143,507	£107,500	-	£2.6m	£0.6m	Mar '09
Southampton	£17.0m	£311,866	£1.43m	£13.9m	£5.6m	£1.5m	Jul '09
Total UK	£51.6m	£2.36m	£3.40m	£20.43m	£35.4m	£10.50m	

Rents - receivable and prospective

In income terms, CareCapital's portfolio is attractive, with a rent roll of £1.3m from its UK properties and £0.65m from the German ones. This gives an overall average rent receivable of £138 per sq. m. including Germany. For the UK alone, where the total occupied space is 12,756 sq. m's. (136,500 sq. ft.), the average rent is £156, compared with a substantially lower German level of £102 (EUR 152), reflecting the lower land values.

In the UK, rentals vary widely across different healthcare categories, although such differences are significantly affected by local factors including land values. CareCapital reports the following variations although the sample base is relatively low for particular categories, e.g. only two dental practices accounting for less than 5% of total floor area.

Rent receivable from different categories		
Rental category	Percent. of total floor area	Rent per sq. metre
Dentists	4.9%	£112.32
Medical practitioners	78.3%	£135.03
NHS Authorities	7.0%	£163.95
Pharmacies	4.7%	£186.51
Other	5.1%	£128.57

High percentage of rent roll to be reviewed before end 2008

The bulk of the rents (77%) are coming from the medical practitioners, and this will remain the case as these are in effect the anchor tenants of all CareCapital's properties. Importantly, despite the young age of the portfolio, CareCapital should enjoy substantial uplifts in its rent receivable in the near term. In 2006, six reviews were completed at an average increase of nearly 15%, amounting to just over £46,000. In 2007, seven properties will be reassessed and, in the following year, a further four. Thus, over the two years, 47% of total rents receivable will be reviewed. The pattern over the next few years is as shown.

Future rent review pattern		
<i>Rent review time table</i>	<i>Rent subject to review</i>	<i>Percentage of total rents</i>
0 -1 year	£558,262	33%
1 - 2 years	£231,500	14%
3 - 4 years	£426,468	25%
4 – 5 years	£74,998	4%
Over 5 years	£416,216	24%

While there is a prospect of early rent increases, CareCapital also has long term security of income due to the lease terms. As shown, only 15% of rents receivable is from leases with a term of fifteen years or less. The typical lease term is now twenty years, but there are some leases of longer duration.

Security of income by lease term	
<i>Period in years</i>	<i>Percentage of total rents</i>
Under 10 years	11.24%
10 – 15 years	3.83%
15 – 20 years	35.69%
20 – 25 years	31.16%
Over 25 years	18.08%

New style leases for new generation properties

Increase in scale if not risk...

The size, scale and risk elements in financing new generation primary healthcare facilities have resulted in the development of new types of lease for GPs and other tenants. Modern integrated, 'fit for purpose' accommodation would generally be outside the financing scope of a tenant who uses only a fraction of the space provided. Local Improvement Finance Trust (LIFT) leases have been developed which are more tenant friendly than typical rack rented institutional leases. Some of their provisions have been incorporated into Third Party Developer schemes (3PD), initiated and procured by doctors, which are fairly commonplace.

Healthcare leases are now generally of the TIR type

Ultimately, from CareCapital's standpoint, the main interest in a property is what net rent can be obtained, what value this equates to on application of the 'healthcare' yield and the likely upside over the term to maturity. Some differences in primary healthcare property leases compared with normal commercial leases are as follows:

- Sourcing an appropriate development site and obtaining planning consent can be challenging because delivery of primary health care is very location specific;
- 3PD schemes are initiated by GPs with the support of PCTs, but there may be other parties in occupation who need to sign side-by-side leases with the developer;
- The Local Health Authority reimburses the rent paid by the GPs, providing a secure covenant;
- The lease term for GPs is usually twenty years, longer than in the commercial office and retail markets, now often ten to fifteen years;
- Leases are increasingly of the Tenants Internal Repairing (TIR) type under which the tenant is responsible for internal repairs and general maintenance and the landlord/developer retains responsibility for structural and external repairs;
- Rent levels are agreed with the Local Health Authority and district valuer, but the review provisions, typically on a three yearly basis, allow for upward and downward adjustment, subject to the requirement that the rent cannot fall below the starting rent.

The UK healthcare property market – government drivers

Increasing government involvement with primary healthcare sector

A key facet of UK Government policy has been the removal of primary health care provision out of the hospital environment to community locations closer to the patient, and the development of alternative provider medical services (APMS). In the latter aim, which is effectively to encourage independent provision, services are restructured so as to offer:

- greater patient choice
- improved access
- greater responsiveness to the specific needs of local communities.

Policy is set out in various DH White Papers

Key factors in the demand for healthcare properties are set out in various Department of Health (DH) White Papers. Primary Health Care Trusts (PCTs) were set up in 2002 to provide and control health care at the local community level, under the strategic Health Authorities which monitor performance and standards. An early initiative was NHS Plan 2000, followed by a Department of Health (DH) White Paper, published in January 2006, 'Our Health, Our Care, Our Say'.

Huge demand growth for both GPs and premises

A huge demand growth for the services of both GPs and specialists has been identified by the DH and British Medical Association (BMA). Recent statistics, in a paper dated..., revealed that primary healthcare was provided by approximately 36,000 GPs in 11,000 surgeries across the UK. The January 2006 White Paper noted that, although a significant increase in the numbers of GPs and nurses had occurred in the past ten years, approximately 10,000 more GPs would be required to cope with the expected demand growth at the primary level. This would be accompanied by a demand for premises - surgeries, walk-in treatment centres and other establishments.

Existing real estate considered 'unfit for purpose'

CareCapital's focus on new build reflects the fact that a large proportion of existing real estate in the primary sector is considered 'unfit for purpose'. Ten years ago, most of the properties from which GPs dispensed primary healthcare were owned or leased by the doctors, but were often in poor condition due to lack of funds for maintenance and still less improvement. In this context, a survey by the BMA in May 2006 indicated that 60% of respondents considered their premises were unsuitable for current needs; a larger majority, 75%, that they would be unsuitable for future needs. As long ago as 2000, a DH survey noted a £3.1bn backlog of property maintenance but, even with restoration/refurbishment carried out, these properties would not meet modern needs.

New vision for the NHS

A fundamental shift of resources is required...

The NHS Plan 2000 started a major shift of financial resources to primary healthcare. Government plans included:

- tackling the backlog of maintenance work;
- replacement and/or refurbishment of primary healthcare properties;
- building and refurbishing of community hospitals;
- new investment of £7bn through PFI deals to build new generation treatment centres for diagnostics and simple operations.

...equal to a 5% transfer from secondary to primary healthcare...

To achieve these plans and extend the range of services - minor diagnostic tests, simple surgery, etc., formerly done in hospital A&E Departments - the Department of Health's January 2006 White Paper stated there was to be a 5% transfer of financial resources (equivalent to £7 billion) from secondary healthcare (hospitals) to the primary level (GPs' surgeries, etc.) each year over the next ten years. The scale of this shift would require significant new investment with the private sector expected to play a pivotal role through PFI schemes although typically their project values are in excess of £25m.

...for investment in new facilities such as 'super surgeries'

CareCapital's strategy is founded on the property dimension of the Government's programme. The DH White Paper highlighted the need for new 'one stop new super-surgeries', of which the targets were 625 by the end of 2006, and 750 by the end of 2008. Super-surgeries are to be 'all-embracing 'medical shops', offering diagnostics, minor surgery and management of long term medical conditions (e.g. asthma and diabetes). They might also incorporate, as appropriate, pharmacies, opticians, midwives, therapists, and social care staff. DH plans also include a commitment to build some fifty hi-tech community hospitals, with specialists in a range of common medical conditions, as found in some other European countries.

The competition

- Several specialist companies emerged in recent years* Between the first half of the 1990s to the early 2000s, more than a dozen companies specialising in primary care properties had emerged. They included Primary Health Properties, Primary Health Care Centres, GP Investment Corporation and Primary Medical Properties. Not all of these still operate under the same names; for example, PMP is now Apollo Medical Partners. Some large operators in the field are primarily property acquirors; others are developers, undertaking the financing and development of medical centres and then, when let, selling them on to investors looking for secure income streams. As with CareCapital, this group builds portfolios for both the income and capital gains prospects.
- PHP is the most prominent...* The most prominent among the ranks of healthcare property companies is Primary Health Properties PLC, an acquirer but not a developer of properties. PHP is a fully listed company with over seventy-five primary healthcare facilities, mainly GPs' surgeries. The Group is managed by Nexus PHP Management Limited and J O Hambro Capital Management Limited.
- ...others include GP Group,...* Other operators are GP Group (formerly the General Practice Investment Corporation Limited), one of the longest established companies specialising in the investment and development of primary care properties, trading under the GPI and GPFM brands. It also manages over £400m of primary care premises and has investment commitments of over £450m in the healthcare property sector. Like CareCapital, it also provides certain management services.
- Assura,...* Assura Group Limited, formerly the Medical Property Investment Fund Limited, is fully listed on the London Stock Exchange. Assura Property Limited, one of the three operating divisions, invests in and develops primary health care property, community hospitals, integrated pharmacy and related medical businesses. At September 2006, Assura Property had invested £385m in ninety-five primary healthcare properties and its target is to commit £750 million by the end of 2009.
- ...and Apollo* Apollo Medical Partners Limited (formerly Primary Medical Properties Limited) has over ten years experience in this sector. In the past four years, it has completed projects valued at £50m and has a further £15m of schemes under construction. As with CareCapital, it sees its role as more than just property development, and seeks to form close working relationships with clients through provision of high quality services and effective long term solutions to meet the varied needs of primary care.

The management team

The Main Board comprises the following:

Dr Michael Sinclair – *Chairman*

Dr Sinclair, who qualified in medicine from the Middlesex Hospital in 1967, has held appointments in teaching hospitals in London. Entering business in 1971, he has held senior management positions with Allied Investments Limited until 1977, and founded the Sinclair Montrose Trust Limited as a private investment vehicle in 1979. In the context of the international healthcare industry, Michael has had senior management positions with companies in both Europe and the USA including Allied Medical Group, Nestor Nursing Homes, British Nursing Association, Lifetime Corporation Inc, Hospital Affiliates International and others.

Paul Stacey – *Chief Executive*

Paul is a qualified Company Secretary and has lengthy work experience in the healthcare sector, being an Executive Director of Nuffield Healthcare Limited. He joined Sinclair Montrose Trust in 1992, and now holds the position of Managing Director, as well as being a director of its primary healthcare development businesses and other associated companies. Paul was instrumental in the establishment of walk-in GP centres in the UK.

Steve Wilden – *Finance Director*

Steve qualified as a chartered accountant in 1975 and has worked in several major organisations including TI Group Plc, Rockwell International Inc and Courtaulds Plc. In 1997 Steve was appointed Group Finance Director of Sinclair Montrose Healthcare Plc, an AIM company which went to a main listing in 1998 before delisting to a management buyout in 1999. In 2000, he left SMT to become Chief Executive Officer of Supporta Plc (formerly Staffing Ventures Plc) before joining CareCapital in 2004.

Non-Executive Directors include Lord Evans of Watford and Keith Gibbs. Lord Evans, who received a Life Peerage for services to charity, was the founder of Centurion Press Group and a director of several companies in publishing and insurance. Keith Gibbs is a mathematician by training and a qualified actuary with wide-ranging experience gained in the healthcare and insurance markets. He was the appointed Chief Executive of AXA PPP Healthcare in 2001 having worked in major life assurance companies such as Sun Life of Canada and Sentinel Life PLC.

Other key individuals have joined CareCapital to provide expertise and experience in healthcare related fields. These include Allan Weiner, with a background in healthcare service operations and screening. Allan co-founded and was the CEO of Euroclinics, a healthcare services company focusing on assessment and prevention of cardiovascular diseases.

Kenn Dalley qualified as an architect and specialises in new project design and property development consultancy; Graham Gardner has a background in surveying and medical property development; and Rick Hayes in business development, site finding, evaluation and planning.

Allan is an executive Director of CareCapital Ltd, the main operating company, Kenn is the Director of Estates and Development, whilst Graham and Rick are Directors of Medical Centre Developments.

Summary and conclusions

<i>Developing is the key</i>	CareCapital is differentiated from other healthcare property companies by being a developer as well as an investor, and initiating projects where it sees opportunities for income growth and capital appreciation.
<i>...and the UK market is expanding</i>	The UK healthcare market is experiencing a major expansion of the primary sector. The DH is planning a major shift of resources to that sector, equivalent to 10% of the budget in each of the next ten years. This shift requires substantial investment in larger premises and CareCapital is capitalising on the domestic opportunity to expand its portfolio of suitable high quality properties of which there are now twenty-one. The asset-backed Company has a diluted adjusted NAV of 21.3p.
<i>...but there are opportunities in Europe...</i>	The industry is an international one with health authorities placing increasing emphasis on community-based, primary healthcare provision. In Europe, some countries such as Germany, have taken these developments further than in the UK and there are excellent profitable opportunities available, at superior yields, with no extra risk. CareCapital has made two initial investments in healthcare properties in Germany.
<i>Net valuation of £24.4m</i>	Total rent rents receivable are £3.9m the bulk of which is currently UK-generated. All have high quality covenants under-pinned by NHS funding requirements. On a conservative yield of 5.5%, the existing estate has been valued at £35.3m and properties under development a further £35.4m. Against the aggregated value of £70.7m there is debt of £46.3m leaving a net valuation of £24.4m at the 31 st March 2007.
<i>First profits achieved</i>	CareCapital has reported first pre-tax profits for the year to 31 st December 2006 of £1.7m including revaluation surpluses of £3.5m (2005: loss of £295,000).

Consolidated Income Statement

For the year ended 31 st December	2005 (Restated)	2006
Revenue	1,747,651	1,832,013
Cost of sales	(72,719)	(83,560)
Gross profit	1,674,932	1,748,453
Administrative expenses	(1,353,167)	(2,352,192)
	321,765	(603,739)
Other operating income	-	251,418
Net surplus on revaluation of investment properties	281,165	3,528,023
Operating profit before exceptional items	602,930	3,175,702
Exceptional costs of AIM listing	-	(589,574)
Operating profit after exceptional items	602,930	2,586,128
Net finance costs	(898,351)	(878,338)
Profit/(loss) before tax	(295,421)	1,707,790
Tax	(1,020,967)	(88,108)
Profit after tax	(383,529)	677,823
Basic EPS (p)	(0.54)	0.93

For the year ended 31 st December	2005	2006
Intangibles	1,751,959	1,751,959
Investment properties	21,427,961	29,517,118
Development properties	64,217	504,916
Other tangible assets	46,868	28,156
Assets held for sale	-	1,500,000
	23,291,005	33,302,149
Current assets - stocks and debtors	380,531	567,160
Cash and financial instruments	6,955,128	2,528,714
Total assets	30,626,664	36,398,023
Current liabilities	(1,170,485)	(1,557,211)
Non-current liabilities	(18,293,513)	(20,760,406)
Other	-	(702,735)
Total liabilities	(19,463,998)	(23,020,352)
Net Assets (= Shareholders' funds)	11,162,666	13,377,671

For the year ended 31 st December	2005	2006
Profit or loss after tax	(383,529)	677,823
Adjustments	680,003	(1,248,438)
Cash flow from operations	296,474	(570,615)
Net interest	(771,523)	(907,419)
Acquisitions of investment properties	-	(6,058,524)
Capital expenditure on development properties	(651,504)	(481,960)
Capital expenditure on plant and equipment	(28,280)	(14,293)
Cash flow before financing	(1,154,833)	(8,032,811)
Financing:		
Proceeds from issue of shares	-	1,458,083
Other		(655,410)
(Incr.)/decr. in debt in year	(178,146)	(1,941,533)
Net (debt)/cash at period end	(7,383,476)	(16,555,147)

Financial Diary		Major Shareholders	
Next events:		<i>From Hemscott & Company announcements</i>	
Half year results	Sep 2007	Sinclair Montrose Trust	27.61%
Next year end	Dec 2007	Solera Holdings	4.34%
Preliminary results	Mar 2008	Canada Life Group	3.69%
AGM	Apr 2008	Henry Lafferty	3.38%

This research may be viewed on www.cityinsights.co.uk

Tony Cooper

May 2007