

# Q2 2006

## LONDON LIFE REAL ESTATE FUND BULLETIN



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The London Life Real Estate Fund was established in 1998. The Fund is invested in 89 high-quality income producing properties, diversified by type and location, with a gross value of \$1.3 billion. The Fund's objective is to provide investors with stable income returns and the opportunity for long-term capital appreciation.



Poco Place, Port Coquitlam, BC

### ACTIVITY

This quarter has seen tremendous activity, primarily due to the acquisition of a large portfolio of retail and office properties. Comprising over 2.3 million square feet, this acquisition substantially increases the Fund's presence in Western Canada in the retail and office markets.

The second quarter of 2006 has been an active and productive one with the acquisition in early June of a 30% interest in the TGS North American REIT portfolio for \$126.0 million. The portfolio includes 20 assets – 10 office buildings with 1.2 million sf of space, nine retail properties totalling 1.1 million sf, and a 3.5 acre parcel of land adjacent to one of the office assets. This established collection of properties has an occupancy level of 96%, expected to grow to 99% by next year, with no more than 14% of the portfolio expiring in any one year. The Fund plans to hold 80% of the properties over the long term. With the balance of the portfolio, the Fund manager will focus on increasing value through leasing renewals and minor capital upgrades. Tenancy is considered to be very strong; the top 20 tenants account for 60% of the net rentable area, 61% of the total net rent and have an average lease term of close to six years.

Assets of the portfolio are concentrated in Calgary, Edmonton and the greater Vancouver area. With above average population growth, employment, per capita income and gross domestic product, these cities are considered to be among the fastest growing in Canada. The Fund, in acquiring this portfolio, is enhancing the quality and stability of its assets, while realizing a strategic goal of increasing its presence in the office and retail markets in Western Canada.

Other activity in the quarter included the acquisition of a 50% interest in 8585 Baxter Place, a prime office/industrial property in Burnaby, British Columbia, for \$2.4 million. This 39,000 sf building, with primary tenants Squirrel Systems Canada and PMC-Sierra Inc., sits on a 2.3 acre site in the Lake City Business Park, an economically robust and strategic location. Another recent Fund acquisition, Production Court, is adjacent to the property and assists the Fund in meeting its objective of achieving operational efficiencies and synergy between assets.



One Executive Place, Calgary, Alberta

## ADDING VALUE

Outperforming national office market trends, 1188 West Georgia – a 20-storey, 204,400 sf Class ‘B+’ office building in downtown Vancouver – boasts a 96% occupancy rate and has increased in value by 29% since acquisition in May 2001. This is a Fund success story!

At the end of 2001, shortly after acquiring 1188 West Georgia, the downtown Vancouver office market was very strong with an overall vacancy rate of 4.1%; this building’s vacancy was 4.3%. Then, as a result of the technology sector fallout and the overall weak provincial and national economy, the greater Vancouver office market went into decline. At its worst, in 2003, the vacancy in downtown Vancouver was 14.5% – three times higher than market lows. Correspondingly, 1188 West Georgia’s occupancy declined to the low/mid 80% range throughout 2002 and 2003.

In response to the changing market, the Fund’s leasing team acted quickly – adjusting lease rates and inducements, creating leasing momentum and focusing positive attention on the building. An aggressive marketing program raised 1188 West Georgia’s profile and resulted in leasing activity in this Class ‘B+’ building when the market was focused on large blocks of ‘AAA’ and ‘A’ class space. The vacancy rate was 7.7% at the end of 2004, compared to the market average of 10.7% for competing Class ‘B’ buildings. As of June 2006, 1188 West Georgia is 96% leased to a well-diversified group of strong tenants with a varied lease expiry profile.

The turnaround in 1188 West Georgia’s occupancy was also a result of the strong fundamentals of the building. Two key elements make it attractive when compared to other Class ‘B+’ buildings: it has excellent amenities, including a fitness facility, showers, sauna and a common meeting room; and it has consistently low operating costs and taxes – something tenants looking for this class of space find very important. Additionally, the Fund manager’s elevator lobby upgrade program, completed in 2004 and 2005, further improved the aesthetics and desirability of the building.

Beginning in 2003, the strong demand for investment grade real estate has driven capitalization and discount rates down across the country. The steady improvement in occupancy and net operating income, as a result of solid leasing and management, has placed 1188 West Georgia in a perfect position to benefit from this market trend. The 2006 appraised value is \$45.5 million, a 29% increase compared to cost at acquisition.

The outlook for 1188 West Georgia continues to be strong in terms of occupancy and value. Certainly this acquisition has been a success for the Fund.



1188 West Georgia, Vancouver, British Columbia



## MARKET OVERVIEW

Real estate values continued to climb in the second quarter of 2006, with key fundamentals pushing markets higher. With demand outstripping supply, we are seeing basic economic principles playing a major role in real estate values this year, as the price investors are willing to pay for quality properties is on the rise.

The Canadian office market remains strong with a prevailing tendency this quarter towards decreasing vacancy rates, creating opportunities for new construction across the country. Toronto, for example, is seeing its first major office project since BCE Place was built in 1992. Calgary and the western market have been in the spotlight recently with vacancy rates nearing an all-time low. These rates may have a tendency to rise slightly in the mid-term due to the supply of approximately two million sf of new space. Office markets in Ottawa and Vancouver are keeping a steady pace, with downtown vacancy rates below 4%, creating a shortage of prime office space. The shortage in Ottawa has led to 1.3 million sf of space under construction. The mining and high-tech industries in Vancouver continue to boost net rents.

The industrial real estate market in Canada this quarter reflects a continuation of recent themes, with western provinces doing very well. Across the country the trend away from older industrial properties to newer, more efficient buildings with higher ceilings and better access endures. Although

the manufacturing industry in Canada may be suffering slightly from an inflated Loonie, this has not yet had any major repercussions for the industrial real estate market across the nation. Vacancy rates remain below 4% in the West; available space is at a premium and has been in decline since 2004. This has created an opportunity for developers, as the market will see two million sf of new industrial space in Vancouver in the coming months. In Ontario, Waterloo is becoming a viable alternative for developers seeking to build industrial space, as development costs and congestion have created major barriers to entry into the Greater Toronto Area.

Retail real estate in Canada has become polarized to some degree in terms of the quality of product on the market. Enclosed community centres and outdated strip malls with deferred maintenance may carry upside, but even with the proper leasing and capital improvements the risks may outweigh the rewards. It will likely be the new format retail centres, including the big box outlet style assets, that will go on to outperform the competition and create the biggest returns for investors. Dominant enclosed regional malls will also remain fully occupied and highly valued for their strong returns.

The multi-family market in Canada is still very strong. The gradual rise in interest rates has inevitably slowed first-time home buyers, including those in the lower-priced condominium market. Despite the low vacancy rates and increased interest rates, very few rental projects are underway. This, in turn, is creating higher demand for existing multi-family assets, leading to an increase in their value. It will be the well-managed properties in desirable locations that will maintain low vacancy rates and offer investors solid returns into the future.



Sterling Place, Edmonton, Alberta

# FUND FACTS

## Annual Return

Year	2000	2001	at December 31				YTD Jun-06
			2002	2003	2004	2005	
Income	6.8%	7.9%	7.7%	7.3%	7.3%	7.2%	3.3%
Capital	4.6%	2.4%	-1.1%	-1.0%	1.2%	8.1%	5.8%
Total Return	11.4%	10.3%	6.6%	6.3%	8.5%	15.3%	9.1%
Total Return to Individuals (net of fees)*	8.2%	7.2%	3.6%	3.3%	5.4%	12.1%	7.3%

\* Fees may vary by client

## Fund Growth (\$ millions)

Year	2000	2001	at December 31				YTD Jun-06
			2002	2003	2004	2005	
Real Estate	\$ 161	\$ 419	\$ 496	\$ 568	\$ 729	\$ 997	\$ 1,203
Cash & Other	\$ 61	\$ 38	\$ 66	\$ 121	\$ 138	\$ 69	\$ 71
Gross Fund Value	\$ 222	\$ 457	\$ 562	\$ 689	\$ 867	\$ 1,066	\$ 1,274
Net Fund Value	\$ 205	\$ 331	\$ 404	\$ 495	\$ 639	\$ 833	\$ 996
Debt/Gross Fund Value	7.7%	28.0%	28.0%	28.2%	26.3%	21.8%	21.8%

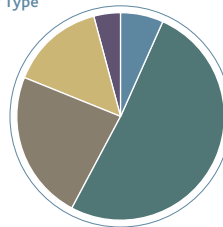
## Vacancy

### By Type

Retail	3.2%
Office	8.4%
Industrial	6.9%
Residential	1.2%
<b>Total by Type</b>	<b>6.4%</b>

## Diversification (Gross)

### By Type



7%	Retail
51%	Office
23%	Industrial
15%	Residential
4%	Miscellaneous

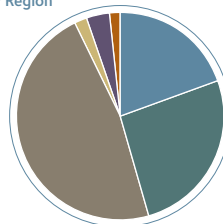
## Vacancy

### By Region

British Columbia	3.5%
Alberta	10.1%
Ontario	5.2%
Quebec	0.4%
Atlantic	16.1%
US	11.2%
<b>Total by Region</b>	<b>6.4%</b>

## Diversification (Gross)

### By Region



20%	British Columbia
26%	Alberta
47%	Ontario
2%	Quebec
4%	Atlantic
1%	US

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