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Report on the Bermuda Commercial Property Market Prepared January 2007



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Introduction

The re-insurance and fund administration industries in Bermuda have seen significant growth since 2000. This has translated into increased demand for commercial property and in turn this has fuelled significant new office development.

Insurance market

Bermuda in 2006 now boasts over 41 insurance companies with over \$500.00 million in shareholders equity. According to the 2005 edition of Standard & Poor's Global Reinsurance Highlights, 14 of the top 40 re-insurance companies or some 40% of the worlds biggest reinsurance companies are now based in Bermuda. The Island is now ranked 4th re-insurance domicile after Germany, USA and Switzerland.

The Bermuda market remains strong. This is despite Bermuda insurers and re-insurers paying nearly 26% of the insured losses arising from the 2005 US hurricane season. This expected payout of \$11 billion compares with an estimated \$7.1 billion losses for US re-insurers. In response to the lost capital and the expectation of high returns from a hardening market in 2006 approximately \$18 billion in new capital flowed into the Bermuda market. Hedge funds now see the local reinsurance market as an investment opportunity. Approximately \$8.0 billion was invested in 9 new start up companies and sidecars to form "the class of 2005".

The number of Bermuda captives has increased steadily since 2000 with the capitalisation expressed in dollar volume significantly up in the period. The introduction of segregated account companies in 2005 saw a further surge in interest in captives using Bermuda's market. The umbrella company with separate cells for separate interests resulted in further incorporations of new companies and has proven to be a growth area for captives by reducing and sharing costs between captives. Bermuda in 2005 had some 987 captive insurance companies and a further 83 protected cell companies containing a further 6,200 cells - still confirming Bermuda as the world's leading captive domicile ahead of the Cayman Islands, the British Virgin Islands, Guernsey, Dublin and the Isle of Man.

The non-captive sector of the Bermuda insurance industry grew out of the US liability insurance capacity crisis of the mid-1980s and was started by pioneering excess liability companies, ACE Ltd. and XL Capital Ltd. Finite risk insurance was added in 1986 with the formation of Centre Re. Then in 1992, on the heels of Hurricane Andrew, Bermuda attracted its first property catastrophe re-insurer, Mid Ocean Re. A further seven "cats" followed in 1993 and with them came a \$4.5 billion influx of new capital being formed within 100 days. These catastrophic re-insurers have now been absorbed by established Bermuda companies as these companies have grown and diversified.

After 9/11 in 2000 a total of 10 new major companies with \$15.00 billion of new capital were incorporated and moved the local market to a new plateau. These Class 4 Insurance companies include such entities as AWAC, RamRe, Endeavour, Axis.

Twelve new companies with a combined capitalization of \$8.00 billion were incorporated after Hurricane Katrina and the 2005 hurricane season. These companies include Arrow Capital; Amlin; Ariel Re; Ascendent Re; Cyrus Re; Flagstone Re; Flatiron Re; Harbour Point; Hiscox (Bermuda); Lancashire; Newcastle and Validus Re. An additional \$10.00 billion in new capital was raised for existing Bermuda re-insurers and sidecars to replace lost capital and re-gear for the increased premium income anticipated in 2006.

Paris re is the new addition to the latest “class of 2006” showing that Europe is not immune to the siren song of Bermuda. Paris Re is an offshoot of the French giant AXA Re with an initial capitalisation of \$1.5 billion.

“Class of 2006”

- Aeolus Re (capital \$500.00 million)
- Castlepoint Holdings (capital \$265.00 million)
- Security Capital Assurance (\$1.2 billion capital)
- Wind River Insurance(owners: Bermuda’s River Capital Group and Aon’s segregated accounts co)
- White Rock
- (SAC)Bermuda)
- Ironshore Insurance (\$1.0 billion)

ACE and XL are giants with combined shareholder equity of over \$21.00 billion. XL or ACE may see a further strengthening as a result of some merger and acquisition activity of Bermuda companies in 2007. Casualty orientated re-insurers from the “class of 2001” likely to include Arch Capital, Platinum Re and Max Re may be targets. The top 20 Bermuda companies now reportedly have a combined total in assets of over \$278.00 billion. The epic storms of 2005, whilst confirming the Bermuda’s market ability to meet the claims from Hurricanes Katrina, Rita, Wilma and other storms, resulted in half a dozen Bermuda companies being taken down including Alea Group Holdings, Olympus Re, PXRE, Quanta Capital, Rosemont Re, sEnergy Insurance and Western General Insurance. Their demise shows the dynamic nature of the Bermuda market with the defaulting companies being acquired or put into run off.

The current trend will see an acceleration of future incorporations in Bermuda as its status as a re-insurance center further increases. This will generate further opportunities for the growth in demand of office rental space.

Office market

This new demand coincided with the addition of extra new office supply and as a consequence there is now an absence of any significant vacancy in the City of Hamilton, which according to 2006 statistics (I) is 2,657,000 sq.ft. Recent completions in Pembroke added approximately 476,000sq.ft. (II) The combined office floor space for the City of Hamilton area therefore totals some **3,650,000 sq.ft.**

- (I) As at July 2006 the Bermuda Government Land Tax Dept. had a total area of 2,407,368 sq.ft comprising 647 valuation units in the City of Hamilton together with an estimated 250,000 sq.ft of Government buildings giving a total of about 2,657,000 sq.ft. for the City of Hamilton.
- (II) The completion of the Waterfront complex Phase 3 on Pitts Bay Road; additions to the Bacardi building; ACE/ XL and other projects added approximately 476,000 sq.ft bringing the total office space in Pembroke to 1,000,000 sq.ft.

Analysis has estimated that some 330,000 sq.ft. was completed in 2006. This space has been largely pre-let or is for the internal growth of existing companies. A further 570,000 sq.ft. of office floor space currently awaits completion in the City and environs. This total addition will represent an addition of some **24 %**. Other properties with outstanding permission for potential development (with planning permission in principle) are appended (Appendix A).

Office Rental growth

Demand for new prime office space from re-insurance companies and fund administration companies have been primary drivers for demand for new office space. The prime rent for good quality office space in newly completed buildings now exceeds \$65.00 per sq.ft. with graduated rents towards the upper floors and penthouses reaching over \$70.00 per sq.ft.

Demand appears to be undiminished and a relative shortage of available space is sustaining the market. Office vacancy rates are negligible and the rate of 4% put forward by the Dept. of Planning in their 1996 Land Use study cannot be supported at present. It is our opinion that vacancy rates are low partially as a result of stringent Bank lending policies on the financing of speculative office developments. This necessitates a pre-letting of 50% to 60% of the created new floor space.

The focus of most new building has a distinct western bias in the City toward ACE, XL, AIG buildings and the Waterfront complex on Pitts Bay Road. The proposal for a new Ritz Carlton Hotel on Par - la - Ville car park demonstrates this bias and if the scheme is completed will provide a business hotel with 100 rooms with 15 shops, 60 residences and 20,000 sq.ft. convention centre to support the Hamilton market.

Commercial Site values

The purchase by the Bermuda Monetary Authority of the Commercial Bank Building on Victoria Street for \$28.60 million in December 2004 represents a new plateau for the Hamilton office market and has fuelled an increase in the values of commercial property. The addition of 24% of new floor space within the next 18 - 24 months may impact on future capital values. Future rental growth may be moderated should the existing level of demand remain the same.

Questions are being asked about Bermuda's environmental capacity and infrastructure. In anticipation of these concerns some existing and new companies

are altering their business model to allow for overseas satellite operations in Halifax, Dublin and Scotland. Active discussion is underway concerning modifications to planning regulations. This may see changes such in the new Bermuda Development Plan as increased height allowances for Hamilton buildings.

The make up of the Bermuda market is likely to swing towards an increased British presence as further Lloyds Agencies diversify or re-domicile their operation taking advantage. The relaxation of term limits on employees has meant that anyone with a professional position can reside here with their families. This will aid recruitment and retention serving to sustain an already inflated housing market. The Bermuda Government seems to be taking some tentative steps to address this housing imbalance having committed to deliver almost 400 units within the next 2 years. The balance of our collective fates is increasingly tied to the success of the insurance sector that dwarfs all other economic activity on the Island with all the indicators showing that its economic development will continue apace.

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APPENDIX A

<u>New Buildings Completed in 2006</u>	
	sq.ft.
AIG expansion, Richmond Road (Sept'06)	120,000
Waterfront Complex Phase 3 (Dec'06)	100,000
AS Cooper (Retail/Offices) Front Street (Dec'06)	65,000
Par-la-Ville Rd./Bda. Commercial Bank (Sept'06)	<u>45,000</u>
	330,000

<u>New buildings currently under construction 2006</u>	
	sq.ft.
East Broadway waterfront (Mar'08)	25,000
Pearman Building-Brunswick Street (Mar'07)	10,000
Washington Properties -Church Street (Dec'2008)	100,000
HWP Front Street (Sept'07)	65,000
HSBC Trimingham's, Front Street (Dec' 2008)	120,000
St. Andrews Church, Church Street (June'07)	45,000
Argus Insurance, Wesley St. (Sept'08)	96,000
Purvis, Victoria Street/Brunswick Street (Sept'08)	<u>110,000</u>
	571,000

<u>Other schemes planned or in discussion</u>	
	sq.ft.
Seon Place, East Broadway	122,000
Ritz Carlton Hotel	120,000
Stonehaven, Reid Street/Court Street	125,000
Bermuda General Bakery, Pitts Bay Road	100,000
CD&P Par-la-Ville Road /Trott Road	90,000
Par-la-Ville Rd (Terceira)	50,000
Par-la-Ville Rd (Pearman)	50,000
East Broadway (Sir John Swan)	100,000
Harbourfront (Front St./Church Commissioners)	35,000
Church Street (Kempe)	50,000
ACE Phase 2	<u>70,000</u>
	912,000

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Rental comparisons 2004

Renaissance Re, Crow Lane House Phase 2, East Broadway - new building of 39,000 sq.ft. gross on waterfront with basement car parking pre-let for 18 years with a rent fixed for 12 years at some **\$60.00** per sq.ft. Completion Sept'2004.

Bank of Butterfield 6th Floor, Reid Street - 1,200 sq.ft. leased at **\$55.00** per sq.ft. 2004.

PXRE Pitts Bay Rd. - New building of some 14,400 sq.ft. nett internal space with single elevator and reduced natural light to lower floors adjacent to road. Rented at an overall rate of **\$58.40** per sq.ft. Jan'2004 (ranging from \$50.00 for lower floors and \$65.00 for upper floors.)

AS&K, Cedar Avenue - 5th floor newly renovated 3,043 sq.ft. sub-let Sept'2004 to Aspen Insurance at \$57.00 per sq.ft. - single elevator corner position natural light on 2 sides.
JLT Insurance brokers rented 23,341 sq.ft. from Jan'04 at **\$45.00** per sq.ft. plus a service charge of \$12.00 per sq.ft.. Extensive upgrading and fit out. Secondary space in location/older building

Rental comparisons 2005

Allied World Insurance, Victoria Street - 26,575 sq.ft. - let at between **\$45.00 and \$55.00** per sq.ft over 3 floors in March 2002 at the peak of the market for 9/11 incorporations . Rent reviews March 2005 to **\$55.00** and **\$65.00** per sq.ft. for top floor.

Astwood Dickinson Bld. 83/85, Front Street - Upper floor of 4,000 sq.ft. leased to R. K. Carvill Insurance Brokers at **\$49.50** per sq.ft. from Sept'05 plus extensive fit out costs for new airconditioning, flooring, walls lighting estimated up to \$1.00 million + / -. 10 year lease.

AS Coopers Building , Front Street/Reid Street- 6th & 7th floors leased June 2005 totaling approx. 10,000 sq.ft. from completion Dec 2006 @ **\$70.00** per sq.ft.. 3 floors available **\$68.00 / \$69.00** per sq.ft.

Maxwell Roberts Bld. Church Street/Par-la-Ville Rd. - New 7 storey building of some 35,000 sq.ft. completion Sept'05 Prestige corner lobby and 2 elevators good natural light from corner location on 3 sides. 3 floors about 16,500 sq.ft. pre-let prior to construction in 2003 at estimated **\$62.00** per sq.ft. completion Sept' 2005. 6th Floor leased to Aspen Re for **\$64.00** per sq.ft. from November 2005

Creative Interiors Bld., 129 Front Street - New letting from 1st March 2005 of 3rd and 4th floors views of the Harbour total area 14,803 sq.ft. rented for **\$62.00** per sq.ft. service charge \$8.00 per sq.ft. plus electricity & taxes.

Cumberland House, City Hall car park/Wesley/Victoria - Rent review 2005 and top floor (7,500 sq.ft.) reviewed to **\$65.00 per sq.ft.** Service charge \$12.00 per sq.ft.

Corner House, Parliament Street - Deloitte rent review established at \$53.50 per sq.ft. for 3 floors totalling 16,073 sq.ft on 1st - 3rd Floors from May 2005

2006 rental comparisons

Par La Ville #19, Hamilton - New Building by Sir John Swan with an area of 33,372 sq.ft fully leased in Feb' 2006 and to be completed in June 2006. Good specification completed for tenant fit out. Raised flooring not provided.

Ground-approx 5,006 sq. ft & First-approximately 5,738 sq. ft. (Bda. Commercial)

Second-approx 5,680 sq. ft. (Validus Re. Ltd.) - \$65.00 per sq.ft.

Third-approx 5,680 sq. ft. (Validus Re. Ltd.) - \$65.00 per sq.ft

Fourth-approx 5,680 sq. ft. (Amlin Bermuda Ltd.) - \$65.00 per sq.ft.

Fifth-approx 5,588 sq. ft. (Starr Int'l. Investments Ltd.) - \$70.00 per sq.ft.

Sterling House, Wesley Street - Older building now refurbished and renovated to a high standard. Mid floor 3,000 sq.ft. leased from March 2006 for \$57.50 per sq.ft..

Cedar House, Cedar Avenue- 3,050 sq.ft. on fifth floor rented at \$57.00 per sq.ft. with a service charge of \$15.00 in addition from March 1st 2006.

Waterfront Development, Phase 3 Pitts Bay Road - New waterfront phase 3 of development - rented to Axis Insurance, Montpelier Insurance and Tokio Marine from 2006 with a total addition of 90,000 Sq.ft. with rates for shell finished structure with a/c, ceiling and lighting ranging from **\$65.00** for ground, **\$68.00** for middle and **\$70.00** for upper floor. 11 Residential penthouses for the Executive market will be completed.

Existing spaces Phase 1 -fitted out by Centre Solutions to an exceptional specification with marble lobby, conceige/security and other amenities-gym underground parking etc. 5th floor - 15,000 sq.ft. fitted space, underground parking, 2 elevators, good natural light with premium paid for fixtures/fittings **\$73.00** per sq.ft. (Nov'2003)

Maintenance/service charge incl. Common lighting, land tax, painting landscaping etc. \$20.00 / \$21.00

Cumberland House, Victoria Street -2,170 sq.ft. on 7th floor rented march 2006 for \$58.40 per sq.ft. with a service charge of \$12.00 per sq.ft. in addition

Creative Interiors Bld., 129 Front Street -1570 sq.ft. penthouse leased at \$62.00 per sq.ft. from March 1st 2006

Richmond House, Par-la-Ville Rd - 18,610 sq.ft. on 3rd / 4th floors of new building (built 1996) rent review April 2006 at \$55.00 per sq.ft. plus 3,200 sq.ft. basement high quality air conditioned storage at \$22.00 per sq.ft.

A.S.Coopers -Reid Street/Front Street - 12,000 sq.ft. rented to XL Group from Dec'2006 for between \$65.00 to \$70.00 per sq.ft.

Bank of Bermuda (HSBC) pre-let 2 floors (approx. 10,000 sq.ft.) prior to commencement of the redevelopment project. (Rents unavailable)

Commercial site values

1. Burnaby Street #10, Hamilton - reportedly sold Mar'2003 for \$1,600,000 for an area of 0.079 ac. with nett income of about \$200,000. Building on 4 floors with elevator and new a/c, services and upgrades.
2. Burnaby Street - Sousa Bld. #5/7, Hamilton - sold July 2004 for \$1.8 million for 0.075 ac. for tenant occupation of upper floor - Rental value say \$175,000 per annum.
3. GE corner property, Front Street - 16,000 sq. ft. warehouse /showroom on a lot of 0.23 ac. Plans for development of 60,000 sq.ft. Sold April 2004 for \$2,920,000 or \$291.50 per sq.ft. Delayed completion for GE relocation to Serpentine Road.
4. Shell Station East Broadway - Reportedly sold for \$2.5 million June 2004 and capable of building 8 residential units or about 27,000 sq.ft. gross offices Waterfront lot of 0.20 ac. Projected asking rents of up to \$75.00 per sq.ft. Site value say \$286.00 per sq.ft. Reportedly sold Sept'05 for \$3,500,000 (\$400.00 per sq.ft.)
5. Just Shirts site, Par la Ville Rd North #9 - Lot of 0.13 ac sold Feb'04 for \$1,300,000 or \$229.56 per sq.ft. on the market 3 years. The right of way encumbrance at the rear reduces the developable area.
6. BGA building, Par-la-Ville Road #19- sold \$3.9 million for redevelopment May'04 for lot of 0.074 ha with an existing warehouse structure. \$489.00 per sq.ft. less the value of the structure.
7. Windjammer Gallery, Reid Street - sold March 2004 for \$1,000,000 for lot of 0.047 ha or \$197.00 per sq.ft. adjoining owner purchaser.
8. Wesley Street #4 / #6 - sold April 2004 for \$2,600,000 for a lot 0.155 ac. \$385.00 per sq.ft.
9. Russell Eve Building , Church Street - sold Nov' 2004 approx. \$5.0 million. Rental income estimated at \$400,000 nett. Yield @ 8.5% Built 1953, lot 0.17 ac Older building with management issues of multiple retail tenants. Building redevelopment proposed.

10. Crawford House, Church Street - sold Nov' 2004 approx lot area 0.1359 ac with rental area of 15,100 sq.ft. built in 1974 leased for \$528,770 pa with small reversion in Oct'05. reportedly sold for \$6.00 million yield approx 8.8% Building redevelopment proposed with adjacent property.
11. Commercial Bank Building, Victoria Street - reportedly sold for \$28.6 million new building of some 50,000 sq.ft. Rental income reportedly over \$2.0 million Bermuda Monetary Authority purchaser. Reflects a yield of @ 7.25% . A special purchaser prepared to purchase as an investment as existing tenancies do not allow immediate occupation , which is normally a requirement for local office purchases. Sold December 2004
12. Burnaby Street #26- BMA Bld. - sold Sept'05 to Bank of Butterfield for \$5,750,000 on a lot of 0.054 ac comprising a building of 11,700 sq.ft. area in total with a lettable area of some 7,145 sq.ft. on multiple floors due to a central atrium/service core. Assuming a rent of \$49.00 per sq.ft. to reflect small suite different floor levels- a yield 6.08% .
13. Trimingham's - #37 Front Street Purchase by Bank of Bermuda from Watlington & Conyers as a result of Trimingham's foreclosure for a site of 0.15 ac. with a modern building intergrated into adjacent property and presenting redevelopment difficulties to the adjacent site. Special purchaser situation April 2005 - \$7,750,000.
14. Trimingham's - #35 Front Street / #4 Reid Street - Purchase by Bank of Bermuda as a result of Trimingham's foreclosure for a site of 0.305 ac in March 2005 for \$10,500,000.
15. Argus / Old Colony site - Wesley Street & Trott Road - Adjoining owner purchased site of 0.70 ac. reportedly for \$11.00 million in September 2006 reflecting **\$360.00 per sq.ft.**
16. Serpentine Road #74 - Quickie Lickie laundrymat site purchased by existing business operator March 2006 for \$2,500,000 for a site of 0.128 ac showing **\$448.00 per sq.ft.**
17. Trott Road #12 - lot of 0.179 ac. sold Jan'04 for \$1.875 million adjoining owner (**\$240.00 per sq.ft.**)