

# Cabinet

23 September 2020



<b>Title</b>	Annual Investment Report (Investment and Regeneration Portfolios)		
<b>Purpose of the report</b>	To make a decision		
<b>Report Author</b>	Heather Morgan, Group Head Regeneration and Growth		
<b>Cabinet Member</b>	Councillor J. Boughtflower	<b>Confidential</b>	No
<b>Corporate Priority</b>	Financial Sustainability		
<b>Recommendations</b>	<b>Cabinet to:</b> <b>Approve the Annual Investment Report</b>		
<b>Reason for Recommendation</b>	<b>The Annual Investment Report 2020 sets out a picture of our investment and regeneration assets as at the end of the financial year March 2020.</b> <b>The report ensures there is full transparency around the portfolio and its performance.</b>		

## 1. Key issues

- 1.1 Cabinet will be well aware of the investment journey that the Council has undertaken in the past four years. Whilst the initial focus was on investments to produce an income to support services to reverse the funding cuts, by 2018 we were in a position to focus on the delivery an ambitious housing programme and regeneration projects. In line with the Capital Strategy the Council's acquisition strategy is now focused on regeneration and housing opportunities rather than income generating assets.
- 1.2 The portfolios objective originally was to generate revenue to support the services delivered by the Council to residents and businesses of Spelthorne. For the past two years it has focused on regeneration and economic development, including the delivery of housing for residents. To reflect this journey, we now have an investment portfolio and a regeneration portfolio, which are covered in different sections in the Annual Investment Report.
- 1.3 With a portfolio of £1bn the Council clearly needs to set out in a transparent way (as any other major institutional investor would) the performance of the portfolio over the preceding year. This Annual Investment Report 2020 seeks to do that (**Appendix 1**).
- 1.4 It is divided into various sections (1) portfolio analysis including property valuation and key performance indicators (2) investment activity (3) market

commentary for both offices and retail (3) Investment portfolio activity including rent analysis - security of income, rent collection and longevity of income (4) regeneration portfolio activity (5) asset management including the Elmsleigh Centre, Communications House, and the Summit Centre (6) retail portfolio including rent analysis – security of income, rent collection and longevity of income and (7) asset profiles of each of our assets including a short summary of the Councils asset strategy for each building.

- 1.5 The report reflects the COVID-19 pandemic which began in March 2020, and the impact that this has had on our portfolio and the wider property market. These impacts were also specifically covered and referenced in the annual valuation report undertaken by Carter Jonas on behalf of the Council which fed into this report.
- 1.6 There is a lot of detailed information in the report, but set out below are some key messages

Portfolio Key Facts	Value
Net Asset Value 31 March 2020	£1.026 billion
Number of Property Holdings	11
Average Lot Size	£93.27million
Total Passing Rent (per annum)	£46.97 million*
Estimated Rental Value (per annum)	£54.28 million**

\* Contracted rent assumes rent free periods have expired, excludes guarantees & Elmsleigh Centre.

\*\*Excludes Elmsleigh Centre.

Key Performance Indicators	Numbers
Portfolio Capital Return (acquisition)	0.86%
Portfolio Capital Growth (last 12 months)	-1.13%*
Portfolio Income Yield at 31/3/2020	5.2%***
Sinking Fund income cover	5.19 months
Investment Cover Ratio	1:5**
Vacancy Rate – % of floor area	8.4%
Vacancy Rate - % of market value/ERV	7.7%***

\*excludes Summit Centre & Elmsleigh Centre

\*\*Investment portfolio

\*\*\*excludes the Elmsleigh Centre

Rent	Value
<b>Annual passing rent (excluding Elmsleigh)</b>	£46.97 million (increase of £3.67 million on 2019)

<b>Acquisitions 2019/20</b>	<b>Value</b>
Summit Centre	£13.785 million current passing rent £1,015,500 per annum
Elmsleigh Centre	£39.325 million gross income of £4,340,107 per annum

<b>Investments</b>	<b>Collection rate 31 March 2020</b>	<b>Collection rate 17 May 2020</b>
Investment portfolio	79%	90%
National average	49.7% all UK rent and 60% office rent	

<b>Retail</b>	<b>Collection rate end May 2020</b>	<b>Collection rate end May 2020</b>
Elmsleigh	18.06% rent	61.13% service charge

#### **Commercial Property Assets – Valuation table.**

<b>Assets</b>	<b>Portfolio</b>	<b>Sector</b>	<b>Value (£m) March 2019</b>	<b>Value (£m) March 2020</b>
BP Campus, Sunbury Business Park, Sunbury	Investment	Offices	389.08	391.73
12 Hammersmith Grove, London	Investment	Office	170.80	165.90
Charter Building, Uxbridge	Investment	Office	135.40	131.20
Thames Tower, Reading	Investment	Office	127.20	126.80
The Porter Building, Slough	Investment	Office	71.40	69.90
World Business Centre 4, Heathrow	Investment	Office	47.00	45.80
3 Roundwood Avenue, Heathrow	Investment	Office	20.55	20.10
Communications House, Staines	Regeneration	Office	15.40	14.50
Elmbrook House, Sunbury	Investment	Office	7.46	7.24
<b>Sub-Total</b>			<b>984.29</b>	<b>973.17</b>

## Properties acquired since March 2019.

Assets	Portfolio	Sector	Value (£m) March 2019	Value (£m) March 2020
Summit Centre, Sunbury	Regeneration	Offices /Ind	N/A	13.50
Elmsleigh Centre, Staines	Regeneration	Retail	N/A	39.33
<b>Sub-Total</b>				<b>52.83</b>

  

<b>Total</b>	<b>All Properties</b>		<b>£984.29m</b>	<b>£1.026 bn</b>
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### 2.0 Options analysis and proposal

2.1 Cabinet can either agree to approve or not approve the report. It is recommended that the report attached at Appendix 1 is agreed.

### 3.0 Financial implications

3.1 The provisional revenue outturn report elsewhere on this agenda sets out the income received from our portfolios which is ~£51.624m gross. After deducting interest payable, principle repayment (MRP) and the sinking fund the contribution to the general budget was £10.146m.

3.2 The Annual Investment Report sets out that despite the COVID 19 restrictions which came into effect on 24th March, by the 31<sup>st</sup> March 2020 the investment portfolio collection rate was 79% and by 14<sup>th</sup> May 2020, 90% of the portfolio rent had been collected (excludes the Elmsleigh Centre). This compares favourably to other landlords; research published by Re-Leased which collated data from 10,000 properties and 35,000 leases indicated that on average 49.7% of all UK rent had been collected 10 days after the March quarter. This was a decline from 69.7% on the average collection rates for the last two years. As you would expect the office sector was more resilient with on average just over 60% collected.

3.2 The COVID-19 effect of rent collection level on the Council's overall financial position was set out in very clear terms in the report on the borough wide response to the COVID-19 crisis to the Emergency Council Meeting on 21 May 2020.

<https://democracy.spelthorne.gov.uk/documents/s27114/Report%20on%20emergency%20response%20to%20COVID-19.pdf>

3.3 Section 8 'Financial Implications' included sections on both commercial income and retail income and stated on the latter "the potential reduction in income from Elmsleigh rents is expected to be around £600,000 (mid-point between the best and worst case scenarios) – most retailers are looking for rental holidays, we are seeking to ensure deferrals instead to ensure that actual write offs are much less than this." However on the Investment portfolio it reported the position as set out in section 3.1 above.

- 3.4 As part of the Council's 'triple net' approach a portion of money has been set aside from each acquisition to be added to a sinking fund. This is to be used when assets come up for lease renewal when it will be necessary to undertake capital expenditure bring them up to the relevant office standards (category A etc) in order to re-let.
- 3.5 As at the 31<sup>st</sup> March 2020 the Council accumulated a sinking fund balance of £20.3m (as at 31 March 2019 the sinking fund balance was £10.6 million). The sinking fund is the equivalent to 5.19 months of the portfolio passing rent. At this level the sinking fund would cover 25 months of the net income payable to the Council. In addition it is projected that further contributions will be made based upon anticipated revenue over the coming years.

#### **4.0 Other considerations**

- 4.1 Risk management is embedded in the work of the team and how they assess all of our assets. The Council closely monitors the financial position of all our tenants and guarantors. The accountancy firm Deloitte provides advice on tenant covenant strength on acquisitions, on large transactions and provides regular financial reviews. In addition the Council subscribes to the Dun and Bradstreet service which monitors the financial performance of the tenants. The monitoring of all tenants is clearly important at the current time.
- 4.2 The lockdown for COVID-19 came into effect the day before quarter day. During this period the government has introduced a number of measures to protect tenants which are set out in the section headed 'Rent Collections' in the report. Whilst this has protected businesses it has to a large extent 'tied the hands' of landlords and limited the options available in respect of legal remedies as a result of withheld rental payments.
- 4.3 The report includes specific commentary on risk distribution and security of income. More detail on the general principles around how we manage our assets (out with COVID 19) are set out in the Asset Management Plan (section 5 Investment Portfolio) which is elsewhere on this agenda. That agenda item also includes an appendix setting out the actions that the asset team have been undertaking in the COVID-19 pandemic.
- 4.4 Equality and diversity is not a relevant consideration in terms of this report.

#### **5.0 Sustainability/Climate Change Implications**

- 1.7 There are no climate change implications. As regards sustainability, the vast majority of our commercial assets are under 10 years old and have been built to meet more rigorous building regulations requirements. As an example, 12 Hammersmith Grove is Platinum WiredScore rated, and a BREEAM Excellent building.

#### **2. Timetable for implementation**

- 2.1 The Annual Investment Report will be published on the Council's website once it has been approved by Cabinet. An easy to read Executive Summary will be provided on the website which will draw out the key information in a digestible form for those who just wish to review the headline facts.

**Background papers: None**

**Appendices:**

**Appendix 1 Annual Investment Report**

**Appendix 2 Executive Summary**