

MID SUFFOLK DISTRICT COUNCIL

COMMITTEE: MSDC Council	REPORT NUMBER: MC/18/14
FROM: Cllr Gerard Brewster – Chair of MSDC (Suffolk Holdings) Ltd	DATE OF MEETING: 26 July 2018
OFFICER: Julia Barker Business Support Manager	KEY DECISION REF NO. CNL03

CAPITAL INVESTMENT FUND COMPANY ('CIFCO CAPITAL LTD') BUSINESS TRADING AND PERFORMANCE REPORT 2017/2018

1. PURPOSE OF REPORT

- 1.1 This report presents the trading activity for CIFCO Capital Ltd following its first full year since the venture was approved. Appended to the report (Confidential Appendix A) is a revision to the business plan which will be presented to each Council for approval in July and will form the basis of trading in year 2.

2. OPTIONS CONSIDERED

- 2.1 Not applicable

3. RECOMMENDATION

- 3.1 Mid Suffolk District Council note CIFCO Capital Ltd trading activity and performance for the year to end April 2018 and approve CIFCO's 2018/19 business plan.

REASON FOR DECISION

To provide Mid Suffolk District Council with oversight of CIFCO Capital Ltd performance and activity in its first year of trading.

4. KEY INFORMATION

- 4.1 The investment strategy for 2018/19 commissioned by the Board and developed by the Boards Fund Manager JLL is designed not only to give strong short-term results but medium and long-term income resilience. CIFCO does not target Capital growth and its projections are not based upon such growth.
- 4.2 This medium to long term resilience is based upon;
- A current average WAULT to expiry of over 10 Years
 - A strategy that balances the portfolio so that a significant number of the assets are 'Core' and liquid
 - A strategy that balances other attributes such as geography, asset class and sector so that resistance to medium and longer-term market stresses in any individual attribute can be mitigated

- A company structure that allows exit from the market by disposal through share transfer rather than individual asset sale *in extremis*

4.3 The 2018/19 Business Plan contains all the elements of the 2017/18 Business Plan approved by both Councils last year. The Plan includes;

- A summary of the full market conditions assessment and revised investment strategy commissioned by the Company's Fund Manager, JLL
- This assessment of the market does not include a specific category for Local Authority investment since in the latest figures (2016) transactions amounted to £2.31 Billion (source: House of Commons Library Briefing Paper No. 08142 February 2018) 0.26% of total UK commercial property valued at £883 Billion. (Source: IPF report 'The Size and Structure of the UK Property Market End 2016 update). Although of passing interest the impact of this small level of activity is unlikely therefore to affect pricing in isolation.
- The JLL market assessment upon which the Plan is based looks at the individual attributes of each asset class targeted by CIFCO including strengths and weaknesses.
- The risks of investment in individual asset classes such as high street retail and the effects of 'clicks not bricks' are implicit in the strategy and the limits imposed on exposure across the fully invested portfolio
- The business plan is not the document to analyse the strengths and weaknesses of individual brand covenant. This is a matter for the Board in its due diligence as those assets arise in the marketplace and for the quarterly portfolio covenant review by Board undertaken independently by fund manager JLL
- The Business Plan incorporates high level financial cash flow back to the Council through loans. CIFCO borrows on a fixed rate so interest rate fluctuations are mitigated. Cashflow and operational finance is dealt with quarterly by the Board alongside quarterly risk analysis
- In addition, the Board's future revisions to its investment strategy are influenced by quarterly portfolio analysis report from JLL. These cover;
 - Investment Guidelines
 - JLL IPD (a UK benchmarking index) Forecasts
 - Tenant Covenant Log
 - Critical Dates Schedule
 - Individual Property Business Plans
 - Tenancy Schedule
 - Arrears
 - EPC Schedule

4.3 Often quoted in the media as an authority on the Council investment sector is Lord Oakeshott. CIFCO Capital Ltd is a private commercial investment company which has a coherent and bespoke investment strategy, revised annually in consultation with its Fund Manager JLL. Lord Oakeshott is the Chairman of Olim Properties, a company that invests in commercial property throughout the UK and as such is a direct competitor of CIFCO Capital Ltd when purchasing assets. Any quotations from him or views that he has expressed might therefore be seen in that context.

5. COMPANY STRUCTURE AND IN-YEAR REPORTING

- 5.1 The Board of CIFCO Capital Ltd ('CIFCO') is responsible to its shareholders MSDC (Suffolk Holdings) Ltd and BDC (Suffolk Holdings) Ltd for the proper performance of the company against the business plan approved by the two parent Councils in April 2017.
- 5.2 Since its first meeting 12 June 2017, the Board meets monthly and has held 10 Meetings to date (between June 2017 and April 2018) to review performance, make new acquisition decisions, appoint corporate advisers and put in place strategies and policies for company governance. A wide range of approvals have taken place covering risk, performance management, governance, acquisitions, delegations and procurement.
- 5.3 Each acquisition is approved in the first instance by the CIFCO Board and reported to each Holding Company Board for further consideration and approval before funds are released. No acquisition can be made without the approval of both Holding Company Boards.
- 5.4 Each quarter the Chairman of CIFCO reports progress at a simultaneous Holding Company Boards meeting. He presents his assessment of company activity during the last quarter and performance data relating to that activity.
- 5.5 Each year, the CIFCO Board revises its annual business plan to ensure that it remains consistent with the market place and emerging risks and opportunities. A revision to its investment strategy is incorporated within the revision and developed with advice from Jones Lang LaSalle Ltd (JLL). The Chairman reports this revision again at a simultaneous meeting of both Holding Companies for consideration and approval before it progresses to both full Councils for final consideration.

6. BOARD DIRECTOR PROFILES

- 6.1 In 2017 the Holding Companies appointed Directors to the Board of CIFCO that offered the Board a Council shareholder perspective (through the appointment of two elected member Directors) but balanced this with a strong commercial property industry expertise (through the appointment of three industry expert Directors not linked to the Council). In combination, the aim was to ensure that business plan targets were understood and achieved. Both Council Directors underwent a mandatory and externally validated skills assessment before appointment. The following individuals have been appointed;



Chris Haworth (Chairman of the Board) - BSc. in Estate Management from Reading University, Fellow of the Royal Institution of Chartered Surveyors, and a member of the National Landlords Association. Partner of Carter Jonas for 12 years, until August 2012, and Head of the National Commercial Division for 8 years.

Henry Cooke - Investment banking professional with over 30 years' experience in roles across research, sales, trading, structuring, origination, syndication and asset management of US, UK, Australian and European mortgage backed, asset backed, whole-business and real estate financing.



Mark Sargeantson - Fellow of the Royal Institution of Chartered Surveyors, Partner of Cluttons, until early 1991. Acted for a wide range of property owners and investors mostly in portfolio and asset management in London and across UK. Joined Fenn Wright, Ipswich in April 1991 and was a partner until 2008 and a consultant to the practice to the present day.

Nick Ridley OBE DL - Elected Member, Babergh District Council - Has been a Babergh Councillor since 2003, Chairman of the Strategy Committee (Leader), Chairman of the Council, Chairman of Planning. Before joining the Council was Chairman of several Statutory and Voluntary Organisations, has had long term experience in Property Development and Property Investment Companies



Derrick Haley - Elected Member, Mid Suffolk District Council - Has been a Mid Suffolk District Councillor since 2003. Held all the major council positions; Portfolio Holder for Finance for nine years, Deputy Leader six years and Leader for four years and Chairman of the Council. Has served as Chairman of various Voluntary Organisations including the CAB and U3A. Held senior positions in the metal industry.

7. CORPORATE GOVERNANCE

- 7.1 In its first year, the Board of CIFCO has adopted the UK Corporate Code of Governance, a strong risk management strategy and continues to scrutinise all its acquisition opportunities with the appointed legal and investment strategy advisers to ensure it meets the criteria required by its Council shareholders.
- 7.2 The Councils' future predicted income as originally envisaged is shown in Appendix 1 of the Business Plan. A loan repayment schedule has been produced by the two shareholding Councils and the income projections for the Councils based upon actual investment to date and predicted income from future investments is shown in Appendix 2 to the business plan once loan documentation is finalised.
- 7.3 The Board has continued existing property management arrangements on acquisition to maintain continuity and ensure a smooth transition of ownership. It is currently however procuring a property management partner for the whole portfolio and this is expected to be completed shortly. It has insured all assets through Zurich Municipal, based on the existing relationship with the Councils. The Board has however commissioned a review of insurance to ensure that its risks are fully covered and that it is achieving market value in premiums paid.

- 7.4 The Board aims to complete full investment 6 Months ahead of the original 18 Month target. This revised Business Plan for 2018/19 lays out how this will be achieved.
- 7.5 The Board's fund management adviser (JLL) provides quarterly advice on the economic outlook upon which the Board, in part, can base its investment decisions. In the most recent financial quarter JLL reported on the national outlook and on individual sector attributes. This outlook data has been used to inform the 2018 investment strategy and is outlined in the Business Plan.
- 7.6 The Board will be requesting from the Councils (via its holding company shareholders) a maximum 10% (£5m) contingency against the full investment previously approved to ensure that it makes its final acquisition in line with the business plan criteria.

8. FINANCIAL PERFORMANCE AND ACQUISITION PROGRESS

- 8.1 The Board has considered the merits of acquiring 46 assets, rejected 36 as unsuitable, submitted offers on ten and acquired six. The Board, with holding company approval, has invested in these six assets valued at £23,572,000. This accounts for almost half of the total funds allocated by shareholder Councils.



- 8.2 From these 6 properties, the company receives £1,410,466 in rental income per annum, which will rise to £1,462,448 by 2022 based on ERV assumptions and known reversions. Once fully invested, the complete portfolio can reasonably be expected to produce rental income of circa £2.8 million per annum based upon the performance of the portfolio to date and assuming the investment market remains broadly similar and full investment is reached.

- 8.3 A summary of the assets acquired and held by the company at end April 2018 are;

36-39 Long Causeway, Peterborough (Completed 18 December 2017)

The property presented a good opportunity to invest in a centrally located asset within the prime retail pitch in Peterborough. The units are well let to strong covenants and both units are let off rebased rents in line with the market, providing an opportunity for future rental growth as the retail market in Peterborough continues to strengthen. This property is let to Wagamama Ltd and Nero Holdings Ltd.

20-25 Kingsway, Norwich. (Completed 14 February 2018)



The property presented a good opportunity to invest in a fully let estate within an established industrial location in Norwich. The units are fully let to a variety of smaller local and regional traders, although risk is spread across 6 separate tenants. 2 have been in occupation since the 1980s.

43-45 High Street, Brentwood. (Completed 15 January 2018)

The property provides a well let, recently refurbished retail unit in an established prime retail location. The long unexpired term and fixed rental uplifts will generate an increasing annual income for the fund with minimal exposure to capital expenditure. Going forward the Brentwood location should also benefit from the soon to open Crossrail transport links. The property is fully let to Marks and Spencer PLC



Greyfriars Court, Milton Keynes. (Completed 31 January 2018)

The property is a well-located asset within an established dealership location. The showroom is let to a good covenant with the additional benefit of a guaranteed lease. The recent refurbishment provides income for an extended period with minimal need for capital expenditure. The building comprises the head office for the Marshall Motor Group Ltd.



2-4 Pasadena Trading Estate, Harlow. (Completed 14 February 2018)

The property is an industrial asset in a south-eastern location. The units are both let to local covenants, although market evidence demonstrates that the acquisition is underpinned by VP values, which are currently higher than the agreed investment value being paid. The strengthening industrial market and lack of competing stock provides a good basis for future rental growth.



Go Outdoors & Lewis's, Princes Gate Retail Park, Harlow. (Completed 23 March 2018)



The property is a retail warehouse within an established south-eastern location. The property provides a good income stream as well as presenting asset management opportunities. The strengthening local market provides a good basis for future rental growth. The property is fully let to 2 tenants, Go Outdoors Ltd and Lewis's Home Retail Ltd.

9. CORPORATE APPOINTMENTS

9.1 During its first year of trading, the Board appointed a range of corporate partners to support its investment activity;

- JLL – Fund Manager and Acquisitions Adviser
- Birketts LLP - Legal Adviser
- Zurich UK - Portfolio Insurer
- Lloyds Bank PLC – Corporate Banking
- Ensors – Accountancy and Financial Audit
- ARK Consultancy Ltd – Asset Acquisition and Co-ordination
- Council's Audit Services – Appointment currently being negotiated

10. RISK MANAGEMENT

10.1 The Board of CIFCO CAPITAL LTD actively manages risk and considers the fund risk register formally at the Board meetings each quarter. There is a comprehensive risk management strategy in place which requires the Managing Director to attend a group risk panel each quarter to report on risk to the Holding Company Chairs and shareholder senior risk officers.

10.2 This report is most closely linked with the Council's Corporate / Significant Business Risk No. 4a – If the Capital Investment Fund (CIF) is not able to generate the investment returns forecast in its Business Plan; income projections for the Councils will not be met. Key risks are set out below:

Risk Description	Likelihood	Impact	Mitigation Measures
Financing and availability of funds that offer returns required.		Cost of borrowing with costs exceeds net return resulting in fund not contributing to the level expected.	Retaining of treasury advisors to fix best rates over investment period. Use of PWLB rather than commercial borrowing arrangements. Flexibility in structure to seek alternative sources of finance if required, Initial modelling of returns includes for fluctuations in cost of borrowing over time. Tax efficient structures being explored by Board including REIT structures

Reduction in opportunities, including through upturn and competition in market, resulting in full fund not being invested		Reduced income in early years.	Acquisition policy allows for regional acquisitions as a norm and national acquisitions in extremis. Current progress shows a pipeline of 47% invested within 6 months of trading commencing. Business plan for 2018 reflects latest realities of market place and adjusts sector and Core, Core Plus split. Fully invested yield still targeted at 6%
---	--	--------------------------------	--

11. REVISED BUSINESS PLAN CONSULTATIONS

11.1 The Board of Directors considered a revision to its business plan in consultation with its adviser JLL for 2018/19 and subsequently approved its revision on 19th April. The Chair subsequently presented the revised plan to both BDC and MSDC Holding Companies on 25th April where it was unanimously approved for presentation and consideration for approval by the two shareholding Councils. This will now take place at meetings in July.

12. EQUALITY ANALYSIS

12.1 An Equality Impact Assessment was originally completed in September 2016. The outcome of the assessment was that the strategy itself will not impact residents, staff or any specific protected characteristics. Funding for the programme is independent of existing revenue streams and therefore it will not impact the delivery of any existing front-line services.

13. ENVIRONMENTAL IMPLICATIONS

13.1 There are no known negative environmental impacts resulting from the proposals within the CIFCO CAPITAL LTD Business Plan 2018/19.

14. APPENDICES

Title	Location
(a) CIFCO CAPITAL LTD Business Plan 2018/19 (CONFIDENTIAL)	Attached