Surrey Heath Borough Council
Executive
17 October 2023

Property Portfolio Update

Portfolio Holder:	Cllr Shaun Macdonald – Leader
Strategic Director/Head of Service	Martin Breeden, Head of Property and Economic Development
Report Author:	Martin Breeden, Head of Property and Economic Development
Key Decision:	No
Date Portfolio Holder signed off the report:	13 October 2023
Wards Affected:	All wards

Summary and purpose

To inform the Executive of the current and projected income and costs associated with the Council's Property Portfolio including some of its major retail acquisitions.

Recommendation

The Executive is advised to note:

(i) the findings of this report.

(ii) the cost of debt financing and repayment funded by the income generated by the Council's property portfolio and any surplus/deficits therein.

(iii) That this type of analysis and reporting will be adopted in future annual performance reports on property related activities to the Performance and Finance Scrutiny Committee.

1. Background and Supporting Information

1.1 Surrey Heath Borough Council has a property portfolio of buildings it owns that have been acquired over a number of years, for purposes of regeneration, provision of civic amenity, municipal benefit, protection of local employment for residents and sustainability of local urban centres.

1.2 Although the properties are not held for investment purposes, there is an expectation that the return across the portfolio provides sufficient income to cover the costs of debt finance (interest) and also provide for the repayment of the debt.

1.3 The property portfolio is managed by the Property and Economic Development team of the Council. The portfolio is split into three main areas: retail property, light industrial/commercial and offices.

1.4 The analysis includes a number of assumptions set out later in the report and seeks to provide a consistent approach across previous years which has been made challenging due to the changes in personnel and practice over this time period period. However, the approach taken in this report provides a good foundation for assessing the performance of the Council's property estate and shaping the approach to transparent reporting going forward.

1.5 This analysis does not include operational property (eg: Surrey Heath House), recreational and leisure properties (eg: Camberley Theatre, Places Leisure) nor community buildings which are primarily leased to community groups and the voluntary sector.

2. The whole commercial sector property estate

2.1 The table below shows the income over the past seven years.

Commercial Sector Income by property type:

	17/18	18/19	19/20	20/21*	21/22*	22/23
	£'000	£'000	£'000	£'000	£'000	£'000
The Square**						
Gross Income	£5,986	£4,104	£2,392	£3,319	£3,935	£3,654
Operational Costs	£0	£0	£9	£4	£1,191	£1,396
Net Income	£5,986	£4,104	£2,383	£3,315	£2,744	£2,257
43-57 Park St.***						
Gross Income	£44	£34	£32	£32	£93	£95
Operational Costs	£40	£40	£40	£40	£40	£40
Net Income	£4	-£5	-£8	-£8	£53	£55

Other Retail						
Gross Income	£402	£948	£446	£141	£146	£455
Operational Costs	£11	£29	£60	£3	£23	£14
Net Income	£391	£920	£386	£138	£123	£441
Internal management costs	-£68	-£70	-£72	-£75	-£77	-£79
Total Retail	**£6,313**	**£4,949**	**£2,690**	**£3,370**	**£2,842**	**£2,675**
Industrial						
Gross Income	**£1,626**	**£2,423**	**£3,103**	**£2,813**	**£2,864**	**£2,878**
Operational Costs	£109	£245	£104	£272	£239	£181
Net Income	**£1,517**	**£2,178**	**£2,999**	**£2,541**	**£2,625**	**£2,697**
Office						
	£632	**£808**	**£2,069**	**£1,593**	**£2,257**	**£1,472**
Operational Costs	£26	£227	£295	£335	£321	£394
Net Income	**£606**	**£581**	**£1,774**	**£1,258**	**£1,936**	**£1,078**
Ind/office internal mgt costs	-£68	-£70	-£72	-£75	-£77	-£79
Total for all Properties	**£8,367**	**£7,638**	**£7,391**	**£7,094**	**£7,327**	**£6,371**

*amended for dividend income (JPUT) due in 20/21 but received in 21/22 (accrual concept)
** Includes the retail properties purchased as part of the original JPUT
*** 43-57 Park St houses the former House of Fraser store and Natwest

2.2 The table below shows the cost of debt financing over the same period:

Cost of overall debt financing

	17/18 £000	18/19 £000	19/20 £000	20/21 £000	21/22 £000	22/23 £000
Minimum Revenue Provision (MRP)	£1,309	£1,400	£2,158	£2,293	£2,355	£2,636
Loan Repayments	£388	£392	£1,346	£3,350	£1,431	£1,782
Interest	£546	£674	£1,444	£1,395	£2,061	£2,752

Total	**£2,243**	**£2,466**	**£4,948**	**£7,038**	**£5,847**	**£7,170**
Net income after financing	**£6,124**	**£5,172**	**£2,443**	**£56**	**£1,480**	**£-799**

2.3 Where there is a surplus of net income over the cost of finance and repayment, then this has contributed to the net cost of Council services and/or contributed to the Council's reserves. One of these earmarked reserves, the interest equalisation reserve, stood at £7.3 million at 31 March 2023 with a planned drawdown in 2023/24 of £2.0 million to offset the current high interest rates. This was agreed as part of the 2023/24 annual budget set by Council in February 2023; the reserve balances are set out in the Medium Term Financial Strategy agreed at the same Council meeting.

2.4 Minimum Revenue Provision (MRP) is an amount set aside for repayment of our Capital Financing Requirement (CFR) and is a nominal amount charged to the revenue account based on assumption of asset life. This will vary based on individual assets.

3. The Square Shopping Centre and 43-57 Park St.

This section looks in more detail at the cost and income profile for the two retail acquisitions made in 2016.

3.1 The properties were acquired for the following acquisition costs:

The Square:	£87.1 million including purchase costs
43-57 Park St.:	£18.5 million including purchase costs

In addition, £7.0 million was incurred in 2017/18 on a refurbishment of The Square.

3.2 The figures have been produced to give an illustration of the income and costs without committing resources to a more forensic historical investigation. For instance, the following assumptions have been made:

3.2.1 That all management and other costs relating to The Square were paid by the Jersey Property Unit Trust in which the asset was held before distribution of dividends until the dissolution of the trust in 21/22.

3.2.2 For direct internal management costs of a full time asset manager has been assumed for each of the retail and industrial portfolios. No accountancy, legal, HR or senior management time has been allocated to the costs associated with property ownership.

3.2.3 Future income for The Square has been produced by making line by line cost forecasts and shop by shop forecasts of letting and lease renewal assumptions.

3.2.4 That the centre refreshment costs were all incurred in line with the £7.0 million budget in 2018/19. In certain situations assumptions have been made as to non-recoverable expenditure. ie expenditure that cannot be recovered through the routine service charge to tenants.

3.2.5 For 43-57 Park St. allowances have been made for the cost of asbestos removal and replacement of the roof but not other works required to re-let the building nor any income for such reletting. This is potentially the least favourable scenario. The council is currently investigating the optimum reconfiguration of the building to secure new occupiers.

4. The table below shows the projected income from The Square and 43-57 Park St. Forecasting for the remaining properties will be undertaken later in 2023.

	23/24	24/25	25/26	26/27	27/28
	£000	**£000**	**£000**	**£000**	**£000**
The Square	£2,409	£2,624	£2,410	£2,264	£2,214
43-57 Park St.	-£102	-£130	-£130	-£130	-£130
Internal mgt costs	-£82	-£84	-£87	-£89	-£92
	£2,225	**£2,410**	**£2,193**	**£2,045**	**£1,992**

5. The table below shows the key projected capital expenditure for The Square and 43-57 Park St. The potential expenditure for future financial years has been reviewed by the Property and Regeneration Working Group but has not been presented to the Executive for approval.

	23/24	24/25	25/26	26/27	27/28
	£000	**£000**	**£000**	**£000**	**£000**
The Square planned maint. inc. roofs	-£74	-£1,784	-£1,068	-£118	-£308
43-57 Park St. inc asbestos removal	-£255	-£2,560	£0	£0	£0
	-£329	**-£4,344**	**-£1,068**	**-£118**	**-£308**

6. Reasons for Recommendation

6.1 This report is part of the Council's efforts to make the costs and income associated with the Council's commercial properties more transparent.

7. Proposal and Alternative Options

7.1 It is proposed that the Executive notes the analysis set out in this report.

8. Contribution to the Council's Five Year Strategy

8.1 Surplus funds above those added to the Council's reserves are used to help support the Council's net cost of services.

8.2 The Council has a robust approach to letting property, filling voids and maintaining a town centre and portfolio carried out by the Council and overseen by the Property and Regeneration Member Working Group. The work has been exemplary given the difficult national economic climate and property market. For instance, as at the end of March 2023, the retail portfolio had a vacancy rate of 5.6% compared with a national average for shopping centres of 18% and the industrial portfolio had a vacancy rate of 1.3% compared with a London and the South East average of 4.2%.

9. Resource Implications

9.1 This report is for noting only and does not include recommendations with resource implications.

10. Section 151 Officer Comments:

10.1 The Council operates a property portfolio to provide regeneration, municipal and civic amenity to residents and protection of local employment and facilities.

10.2 It is recognised that at times not all parts of the portfolio will generate a return that covers the cost of management, maintenance and debt financing; a view over the entire portfolio should be taken and use of equalisation reserves should also be considered to smooth the impact of higher costs on the local taxpayer.

10.3 The full impact of any valuation changes on property assets will only be recognised when these gains or losses are crystalised on disposal.

10.4 Debt facilities incurred by the Council are based on its continued cashflows as a tax raising body and is not held against individual assets. The Council borrows on the strength of the UK government's sovereign rating and not its asset base. The timing of borrowing is incurred when the balances held by the Council dictate and is based on the Capital Financing Requirement; therefore debt liability is not always concurrent with acquisitions.

11. Legal and Governance Issues

11.1 There are no legal implications arising from this report.

12. Monitoring Officer Comments:

12.1 There are no matters arising.

13. Other Considerations and Impacts

Environment and Climate Change

13.1 The Council's property estate forms part of the carbon footprint of the Council and the borough. Work is taking place through the Climate Change Working Group to improve the energy efficiency of Council buildings where feasible and to increase the use of green energy generation.

Equalities and Human Rights

13.2 Although this report deals with the Council's commercial property estate, the Council also owns a range of community buildings, many of which are used by charities and voluntary sector organisations that are working with some of the most vulnerable and disadvantaged in the local community.

Risk Management

13.3 Past financial performance cannot be taken as a guarantee of future financial performance across the portfolio.

13.4 The Council's cost of borrowing will continue to fluctuate with changes in prevailing national interest rates. This is managed by the Council's treasury team in accordance with the agreed Council strategy.

13.5 The Council has put in place a property team with the necessary expertise and processes to effectively manage its property estate and has provided effective oversight through the Property and Regeneration Member Working Group.

Community Engagement

13.6 The Council will engage with local residents and stakeholders on its future strategic vision for the Town Centre and the development on its future regeneration schemes.

Background Papers

None