

Date: 6 October 2021

Item: Funding Update on TTL Properties Limited

This paper will be considered in public

As provided for under section 100b(4)(b) of the Local Government Act 1972, the Chair is of the opinion that this item should be considered as a matter of urgency. The reason for urgency is to allow for the latest information available to be provided.

1. Summary

1.1 This paper provides a summary of the work undertaken since the meeting of the Committee on 23 June 2021 on the property workstream of the Financial Sustainability Plan (FSP) and the wider activity to operate TTL Properties Limited (TTLP) as a dedicated commercial property company within Transport for London (TfL). The paper will set out progress on:

- (a) discussions with HM Government on the FSP property workstream;
- (b) the TTLP business plan; and
- (c) initial market testing on funding options for TTLP.

1.2 A paper is included on Part 2 of the agenda, which contains exempt supplemental information. The information is exempt by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972 in that it contains information relating to the financial and business affairs of TfL. Any discussion of that exempt information must take place after the press and public have been excluded from this meeting.

2. Recommendation

2.1 **The Committee is asked to note the paper and the supplementary information on Part 2 of the agenda.**

3. Discussions with HM Government on FSP

3.1 As was discussed by the Committee on 23 June 2021, the funding agreement with Government dated 1 June 2021 contained condition 10a:

“TfL to agree a plan for housing delivery through a dedicated commercial property company that meets the shared ambitions of the Mayor and HMG to deliver housing in a high demand area and to provide an increased revenue stream. The plan will be agreed between TfL and HMG by June 11 and include a clear milestone for housing to be delivered by the end of 2024.”

- 3.2 In assessing how to meet the condition to deliver housing and increased revenue to TfL, Government and TfL officials discussed proposals that delivered between 10,000 and 50,000 homes depending on the level and timing of any housing grant. Options were present Government on 11 June, and these options were summarised in the paper that the Committee noted on 23 June.
- 3.3 Subsequent discussions between TfL and Government focused on how to drive delivery of the maximum number of homes with the minimum requirement for Government grant funding. Subject to ongoing discussions with Government and TfL approvals, agreement has now been reached on an outline plan that will see TTLP aim to start on the sites that deliver 20,000 homes over the next 10 years. This plan currently assumes no Government grant funding and forms the basis of the TTLP New Baseline Plan that is described below.
- 3.4 Government has set out two additional conditions as part of that agreement. First, TTLP should maximise the use of Modern Methods of Construction (MMC) for its residential development, such that TfL should ultimately seek to deliver over 90 per cent of its homes utilising MMC. Second, TTLP should support Custom and Self-build (CSB) housebuilding.
- 3.5 MMC covers seven distinct categories of innovative construction techniques generally involving off-site manufacture or assembly. These techniques are defined in the report 'Modern Methods of Construction working group: developing a definition framework'¹ (2019) published by the Ministry of Housing, Communities and Local Government (MHCLG).
- 3.6 Though innovate, the benefits of MMC are increasingly well established and include faster pace of delivery, improved safety, increased sustainability, better quality control and reduced traffic movements. Subject to the detail of the agreement, extending the use of MMC is considered likely to decrease delivery risk. The Mayor of London's New London Plan and Housing Strategy both express strong support for "precision-manufactured housing" (i.e. MMC). TfL's published Financial Sustainability Plan explicitly set out the opportunity to leverage TfL's long-term property programme to unlock investment in MMC to accelerate the pace and sustainability of housing delivery, particularly if this is accompanied by investment in construction skills.
- 3.7 CSB cover a spectrum from projects where people build or manage the construction of their home to projects where individuals commission their home, making key design and layout decisions, but the home is built ready for occupation. The Bacon Review² (2021) sets out benefits of CSB, including diversifying the housing market and delivering improved quality and environmental performance. TfL is already bringing small sites to market through the Greater London Authority's (GLA's) 'Small Sites, Small Builders' portal – and opportunities for CSB will now be identified and prioritised through that route.

¹ <https://www.gov.uk/government/publications/modern-methods-of-construction-working-group-developing-a-definition-framework>

²

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1013928/Bacon_Review.pdf

3.8 Discussions between TfL and Government officials have been positive with broad agreement on the principle that TTLP should deliver a 'double bottom-line' of housing and income growth returned to TfL in the form of a dividend. There is agreement also that TTLP should be a self-financing enterprise wholly owned by TfL, delivering a mixture of for-rent and for-sale housing, with a balanced portfolio of activities to optimise sustainable financial returns over the long-term.

4. TTLP Business Plan

4.1 At the meeting of the Committee on 23 June 2021, the three main business plans scenarios for TTLP were shared. These were:

- (a) **Plan X** – a “capital-neutral” budget adjusted to TfL’s current financial restrictions, delivering 10,750 homes with reduced capital investment in existing assets and development programmes deferred so that funding from disposals is received before development expenditure is committed;
- (b) **Baseline Plan** – TTLP’s then default plan delivering 13,278 homes, assuming access to commercial debt funding and including well-progressed commercially viable projects with a focus on developing and holding assets in the long term – but with no allowance for grant funding to bring forward currently unviable projects; and
- (c) **Housing Growth Plan** – adding 61 known projects that are considered, subject to further feasibility, to be commercially unviable (i.e. requiring support in the form of grant) to enable TTLP to deliver 46,350 homes with a corresponding increase in the requirement for funding in the later years of the plan.

4.2 Following the outline agreement with Government, a “New Baseline Plan” has been developed based on TTLP starting on the sites that deliver 20,000 homes over 10 years with an assumption of no Government grant funding.

4.3 As can be seen in Table 1 and Chart 1 below, the New Baseline Plan projects that the annual return to TfL will increase from £6.0m in 2021/22 to £155.7m over 15 years. Over the same period, the value of TTLP’s property assets are projected to rise from £2.22bn in 2021/22 to £4.46bn in 2035/36. This rise is the net result of additional value in existing assets, additional value from newly developed assets and the loss of value from sites that have been disposed of during this timeframe. All of this is delivered without any requirement for investment from TfL, funded instead by commercial debt that is also non-recourse to TfL. Peak debt is forecast to be almost £520m in 2029/30, though the debt in the first three years remains modest at less than £75m.

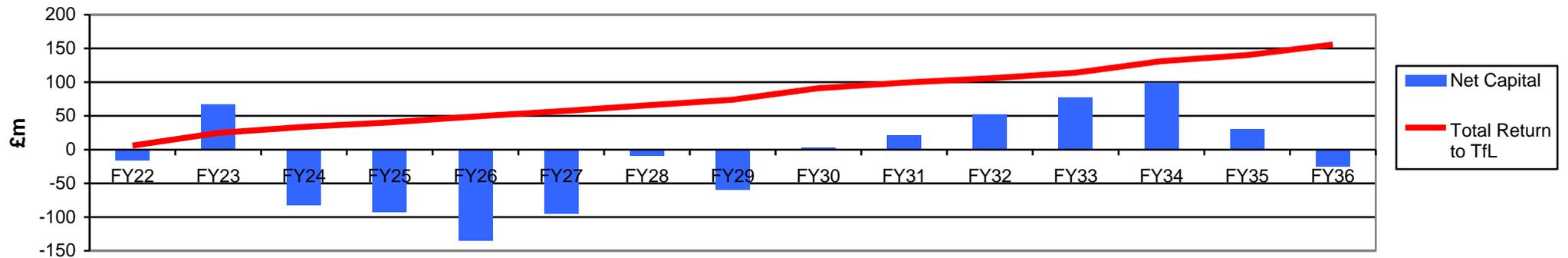
4.4 Further work will be undertaken on the New Baseline Plan in the weeks ahead, both to reflect the emerging Investment Strategy and Asset Plans (see paragraph 4.6 below) and to assess how increased returns to TfL can be delivered in the early years of the plan when TfL’s funding position is particularly acute, whilst maintaining sufficient investment to keep delivering the double bottom-line.

- 4.5 This New Baseline Plan will see TTLP deliver all the residential development projects in the previous Baseline Plan along with the most viable of the sites in the Housing Growth Plan. There is more work to do to establish the optimal design that is both viable and deliverable on these additional sites, and detailed feasibility work will commence as soon as funding becomes available. The feasibility work will be completed jointly with the operating businesses in order to ensure transport benefits are identified and included from the outset.
- 4.6 TTLP has appointed leading property advisor Savills to support the work on the new TTLP Business Plan. Savills is assisting TTLP in the production of a revised Investment Strategy and Capital Allocation Plan. These documents set the top-down context for the Business Plan. Alongside these, new Asset Plans and a Project Prioritisation Framework will ensure the Business Plan is also based on a detailed, bottom-up analysis of existing assets. Savills' work includes an independent review to ensure TTLP's assumptions are fully market facing.

Table 1: TTLP New Baseline Plan

£m	FY22	FY23	FY24	FY25	FY26	FY27	FY28	FY29	FY30	FY31	FY32	FY33	FY34	FY35	FY36
Capital Expenditure	80.3	239.7	303.4	218.3	241.8	224.2	142.6	81.9	152.2	107.7	98.9	139.3	57.2	76.2	54.0
Capital Income	64.2	293.0	220.2	124.0	102.7	106.8	109.7	4.6	155.2	128.7	150.3	180.5	118.6	99.6	21.9
Net Capital	16.1	66.9	82.5	92.4	134.5	95.0	8.9	59.7	3.0	21.0	51.4	77.7	99.3	29.6	25.1
Cumulative Net Capital	16.1	50.8	31.7	124.1	258.6	353.7	362.5	422.2	419.3	398.3	346.9	269.2	169.9	140.3	165.4
TTLP Profit	0.0	0.0	0.1	0.2	0.3	0.4	0.4	0.5	0.5	0.5	0.5	0.4	0.3	0.3	0.3
Net Debt	41.4	0.0	73.1	176.5	318.8	422.7	440.4	509.3	518.4	504.6	464.7	394.8	306.7	287.1	324.1
Total Returns to TfL	6.0	24.7	33.7	40.3	49.2	57.1	65.7	73.9	91.0	99.3	105.8	114.1	131.1	140.1	155.7
Asset Value	2,221	2,158	2,219	2,373	2,671	2,911	3,028	3,115	3,246	3,301	3,467	3,676	3,878	4,093	4,462

Chart 1: TTLP New Baseline Plan - Net Capital and Total Return to TfL



4.7 Once completed, the final versions of the Investment Strategy, Capital Allocation Plan and Business Plan will be shared with the Committee.

4.8 The emerging Investment Strategy is set out below:

	Short Term	Mid to Long Term
Retail	Support post-COVID recovery and consider targeted investments in Zones 1 and 2.	Improve in-station retail and rationalise secondary out-of-station retail.
Arches	Refurbish, re-purpose and undertake minor redevelopment on key arches.	Substantial redevelopment of major arch projects.
Commercial Offices	Retain and invest in core office buildings where these are held as part of wider landholdings around transport nodes. Review options to dispose of non-core assets.	Substantial redevelopment of commercial over station development sites.
Residential	Support development phase of Build to Rent portfolio to deliver additional homes and income.	Review options to exit secondary stock. On-going management and future Build to Rent opportunities.
Car Parks	Manage income from existing contracts. Devise appropriate interim uses prior to re-development.	Redevelopment of car parks alongside future uses and electric vehicle charging.
Long Leases	Protect existing long leasehold and income.	Review long-term redevelopment options and identify any opportunity for additional long-term income sources.

4.9 The diversity of TTLP's asset base is considered a strength, as is the predominance of Small and Medium Enterprises (SMEs) on TTLP's estate. The unique character of TTLP's portfolio will not therefore be fundamentally altered by this work.

5. TTLP Funding and Financing

5.1 The paper to the meeting of the Committee on 23 June 2021 set out how TTLP had worked with Deloitte to review potential funding options to meet TTLP's capital requirements. All shortlisted options saw property assets consolidated into TTLP, with TTLP having a separate profit and loss statement (P&L) and balance sheet, and its own financial and management accounts focused on commercial development activity with borrowing independent from wider TfL. The review concluded that commercial debt financing by TTLP was the preferred route.

5.2 TfL selling equity in TTLP in the market was quickly discounted as any equity sale now would inevitably be at a discount to the expected growth in asset value, and so would not meet TfL's best value obligations. TfL corporate debt was similarly discounted as it would not provide the necessary independence from wider TfL

borrowing and would have constrained TfL's future ability to borrow to fund transport projects. TTLP unsecured debt with either GLA or HM Government guarantee was attractive but considered unlikely to be available, and this indeed has proved to be the case.

- 5.3 Non-recourse debt secured on TTLP's asset base – i.e., debt secured against TTLP assets, so that, if required, lenders could seize the assets the debt is secured against, but cannot seek any further compensation from TfL – was considered the most viable option at the time. Assuming it could be obtained at a reasonable price, unsecured non-recourse debt was however recognised as a potentially more attractive alternative.
- 5.4 We have since undertaken soft market testing in order to assess potential lender interest and identify any constraints associated with the proposed TTLP structure to inform the approach to the financing strategy.
- 5.5 Initial discussions have taken place with a number of lenders, including UK clearing banks, European banks and institutional investors. All conversations to date have been based on either publicly available information, including the paper to the Committee on 23 June 2021, or non-sensitive information that could be made public. As a result, all feedback provided by lenders is strictly subject to further information being available.
- 5.6 That said, the initial feedback from lenders has been very positive and no concerns have been raised about the financeability of the structure proposed by TTLP. Given the format of TTLP's business model, there could be a number of financing options available. Initial indications suggest that it could be practical to cover the first few years of funding requirement via a committed bank facility that can be drawn as and when the funds are required. As the financing requirement increases, the amounts drawn under the bank facility would be refinanced with an alternative source of debt.
- 5.7 While it is very likely that in the medium to long term a secured debt solution would provide better value for money, it appears possible to set up an initial credit facility on an unsecured basis, subject to certain financial due diligence and covenants. An assessment of available financing options is being undertaken ahead of finalising our approach for going to market. Further, commercially sensitive, detail is provided in the paper included in Part 2 of the agenda.
- 5.8 The agreement with Government would increase the overall debt level across the Group. Corporate Finance considers the additional debt to be affordable, particularly in the context of the nature of the debt and its role in driving substantial asset value growth and additional long-term income from TTLP's property activity.
- 5.9 To support the assessment of TTLP's robustness, including its ability to support any debt requirements and related covenants, viability testing is currently being undertaken. This testing aims to assess TTLP's long-term financial robustness under several stress scenarios and assess ability to absorb or manage plausible "what if" downside scenarios. Under each scenario financial performance will be assessed against key financial metrics in the form of anticipated covenants and qualitatively in the form of available management mitigations.

- 5.10 At its meeting on 10 March 2021, the Committee approved the grant of Procurement Authority for a 25-year, interest bearing loan of up to £2.1bn by London Underground Limited to Transport Trading Limited, to fund the acquisition of ordinary share capital in TTLP. The dividend paid by TTLP will, amongst other things, enable the servicing of this loan. In doing so, TTLP will follow normal commercial principles (whilst still adhering to all Mayoral and TfL policies). This will require TTLP to deploy capital to meet agreed financial metrics to generate a return that both services TTLP's own debt and delivers a growing dividend to TfL.
- 5.11 Following the completion of stress testing, we will start taking active steps to prepare TTLP for borrowing on a non-recourse basis.

6. Business Update

- 6.1 Progress continues on TTLP's existing development sites. Having secured a £12.7 million Green Development Loan from HSBC, construction is well underway on the first phase at Kidbrooke in our joint venture with Notting Hill Genesis. This first phase of the scheme comprises 413 London Affordable Rent, shared ownership and private sale apartments. In total, 619 homes will be built – with 50 per cent affordable housing.
- 6.2 At Blackhorse View, sales have been progressing well ahead of schedule with 108 sales and reservations taken worth £46.7m. To date, 35 residents have moved in.
- 6.3 Planning remains the biggest risk to TTLP's housing delivery, and this has been particularly felt on our 100 per cent affordable schemes. On 28 July, Harrow Council planning committee unanimously voted to reject a scheme at Stanmore station car park brought forward by our partner Catalyst Housing. The Stanmore scheme would have delivered 277 homes and significantly improved accessibility for users of the station.
- 6.4 This follows the earlier decision by Harrow Council planning committee to reject officers' recommendation and deny permission for 118 affordable flats on Canons Park station car park in another Catalyst Housing scheme with TTLP. A planning appeal was submitted by Catalyst Housing on 8 July and the public inquiry is now scheduled to start on 2 November 2021.
- 6.5 At Sudbury Town, an appeal hearing took place on 23 June 2021, following Brent Council's refusal of a 100 per cent affordable scheme delivering 52 homes proposed by our partner Pocket Living.
- 6.6 More positively, at Arnos Grove, London Borough of Enfield has confirmed that it will not now defend at Inquiry its refusal of our planning consent for 162 homes. The Public Inquiry is currently still scheduled to start on 9 November 2021, with a decision expected in early 2022.
- 6.7 Finally, it was very encouraging to note that TTLP's construction skills programme met the Department for Education's (DfE's) target to support 400 people into work in the last 12 months. It is particularly positive that at least 350 of these people have been in work for over three months and are expected to remain in

sustainable employment. The DfE's Construction Skills Fund Programme ended in September, with final outcomes confirmed the following month.

7. Conclusion and Next Steps

- 7.1 Significant progress has been made since the update to the Committee on 23 June 2021. Subject to ongoing discussions with Government, agreement has been reached on the housing target. This agreement allows TTLP to move from three potential business plan scenarios to a single plan that will be further refined in the weeks ahead to take into account both TfL's detailed requirements and the output of the work with Savills.
- 7.2 Similarly, the soft market testing with UK and European banks and institutional investors has allowed TTLP to confirm previous assumptions and move forward on the basis of a single preferred funding option for the initial years of the plan.
- 7.3 Taking debt funding into account, the latest version of the TTLP Business Plan shows the annual return to TfL increasing over 15 years from £6m to over £150m. It also shows the value of TTLP's property assets doubling to £4.5bn over the same period. All of this is delivered without any requirement for investment from TfL.
- 7.4 Good progress is being made on the financial stress testing of the new entity. An Affordability Report is currently in production and this will be shared with the Committee to accompany the TTLP Business Plan.
- 7.5 In starting on the sites that will deliver 20,000 homes over 10 years, TTLP will have a material impact on the housing sector in London, particularly given TTLP's focus on MMC and construction skills, building on positive work undertaken to date.
- 7.6 More remains to be done over the course of the next six months to refine TTLP's Investment Strategy and Business Plan. These will be brought back to Committee for approval. In parallel, approvals will be sought for the timing, quantum and mechanism for any debt funding, clearly setting out the implications and risks of such funding.

List of appendices to this report:

A paper containing exempt supplemental information is included on Part 2 of the agenda.

List of Background Papers:

None

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