

Date: 28 June 2023

Item: **TTL Properties Limited Valuation Results and Capital Receipts Programme Update**

This paper will be considered in public

1 Summary

- 1.1 This paper provides an overview of the year-end valuation for TTL Properties Limited (TTLP). The valuation process is conducted by a third-party specialist. This paper refers to TTLP assets only, as at 31 March 2023.
- 1.2 In addition, this paper provides an update on the TTLP Capital Receipts programme, which is critical to the capital recycling process core to the TTLP business plan.
- 1.3 A paper is included on Part 2 of the agenda, which contains exempt supplemental information that is exempt from publication by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972, in that it contains information relating to the business and financial affairs of TfL, that is commercially sensitive and likely to prejudice TfL's commercial position.

2 Recommendation

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

3 Context

The Process

- 3.1 TTLP undertakes an annual independent valuation of its investment portfolio. The valuation date is 31 March each year and is carried out by external valuation specialist CBRE, a global leader in commercial real estate services and investment.
- 3.2 The valuation process focuses on assets held by TTLP for commercial investment purposes, that is, income-generating assets. These are represented by seven core sectors: Retail, Office, Arches, Residential, Car Parks, Industrial and Infrastructure.

- 3.3 The valuation process excludes assets of little to no value, ranging from leases, licences and easements at a peppercorn to land parcels below 0.1 acres.
- 3.4 The valuation process does not include TTLP's development joint venture interests, for example at Earls Court – these are valued separately at Joint Venture level and are recognised separately to the investment portfolio of TTLP's balance sheet.
- 3.5 The valuation is driven by asset specific and market information. This includes recent market transactions, occupational information, lease details and asset plans. Dependant on the asset class and use, an appropriate valuation methodology is applied in line with the prevailing market practice.
- 3.6 To ensure robustness and meet accounting requirements the valuation output and process are audited by an external accounting practice, in line with the wider process undertaken by Transport for London (TfL).

The Market

- 3.7 Throughout the past 12 months, the real estate market has been significantly influenced by various factors. Primarily, global inflation has driven a substantial increase in interest rates. This has led to increased project costs and target return rates, as government gilts (a proxy for risk free return) have also risen.
- 3.8 While these market shifts have impacted the industry, certain sectors have felt their effects to a greater extent – most notably secure long income streams, secondary office and industrial. Appendix 1 - CBRE Monthly Index (March 23) illustrates the broader and sector level market movements.

4 TTLP Valuation – 31 March 2023

- 4.1 Table 1 - TTLP Investment Portfolio valuation at 31 March 2023

	Market Value as at 31 March 2023 £m	Market Value as at 31 March 2022 £m	Surplus/ (Deficit) £m	FY valuation change %
Valuation	1,505	1,466	39	+ 2.7
Like-for-Like	1,361	1,456	(94.5)	- 6.5
Passing Rent	61.9	61.8	0.1	+ 0.1
Rental Value	92.5	91.0	1.5	+1.7

- 4.2 The total value of the TTLP's investment portfolio at 31 March 2023 is £1.505bn. This is a year-on-year increase of £39m (+2.7 per cent) on 31 March 2022 figures. Over the year 2022/23, £144m of new assets have been transferred into TTLP, resulting in the valuation uplift.
- 4.3 Adjusting for the new asset transfers, the like-for-like, year-on-year value reduced by £94.5m (-6.5 per cent), while the Passing Rent increased slightly by £0.1m pa (+0.1 per cent) illustrating the shift in value being driven by changes in investor appetite and capitalisation yields.
- 4.4 The CBRE Monthly Yield Index (March 2023) is provided at Appendix 2. This illustrates the yield volatility over the past 12 months, particularly in the industrial sector (where there were yield movements of 175 basis points) and secondary office market (with yield movements of 225 to 300 basis points).
- 4.5 Almost all real estate investment trusts (REITs) and other property companies have seen downward end-of-year valuation results. For the most part, these organisations have had a larger year-on-year downward movement than TTLP's 6.5 per cent, with numerous organisations seeing a double-digit reductions in like-for-like valuations. TTLP's relatively modest reduction is a result of the diverse and granular nature of our portfolio and a lack of exposure to those sectors most severely impacted.
- 4.6 We are currently preparing a benchmark list of equivalent real estate companies against whom we will track annual performance and valuation movements. This will be brought to the Committee in due course and used to track performance against the market.
- 4.7 To create improved year-on-year benchmarking, we are also seeking to move to a bi-annual valuation process during this financial year. This will allow us to gather more frequent and accurate data for comparison and analysis. By conducting valuations twice a year, we can better track performance trends and make more informed decisions based on real-time market conditions.
- 4.8 Some 52 per cent of TTLP's investment portfolio value is held in just 20 estates (an estate being a contiguous collection of properties, generally located around a transport node – Baker Street and Victoria being examples). While comprising 52 per cent of the value, these 20 estates represent only 15 per cent of the total properties held by TTLP.
- 4.9 In line with the TTLP Investment Strategy, the valuation demonstrates the potential for future value increase by investing in the most valuable assets. They offer strong short-to-medium term value-add opportunities. Indeed, some are long leasehold interests with limited intervention opportunities, further adding focus to the remaining limited number of high-value estates in this list.
- 4.10 A key workstream for the next 12 months is to deliver asset plans and strategies for unlocking this value at these high-value estates.

- 4.11 The concomitant outcome of having a large proportion of the portfolio value in a relatively small number of estates is that TTLP's portfolio also has long 'tail' of low value assets. Rationalising this is a core part of the TTLP Investment Strategy, described further in section 5 below.

5 Capital Receipts Programme

- 5.1 TTLP has a diverse portfolio, with high-value, well-positioned assets across London as noted in paragraph 4.8 above.
- 5.2 The portfolio was created organically over a significant period and has only recently been brought under single management, allowing TTLP to review which assets to retain, invest in and dispose of.
- 5.3 The core principles of TTLP's Investment Strategy still hold in the current challenging macro environment. There are focused areas where TTLP needs to evolve over the next twelve months.
- 5.4 To drive operating efficiencies across the portfolio, the TTLP Business Plan includes a strategic capital receipts programme. As well as providing income to reinvest, this enables a more efficient management approach of rationalising assets that do not align with TTLP's Investment Strategy, for example, disparate assets in low-growth sectors.
- 5.5 TTLP aims to diversify and improve the quality of its income. Over the last twelve months, TTLP has introduced a sector-led operating model responding to the Investment Strategy. A sectoral structure enables a focus on a strategic-led target portfolio weighting.
- 5.6 The Investment Strategy sets out a high-level, sector-level investment focus:

Sector	Invest/Retain	Rationalise/Divest
Retail	In-station retail Zones 1 to 3 (incl. Elizabeth line) Out-of-station retail close to transport hubs and in central locations	Out-of-station retail Zones 4 + not near transport hubs
Residential	Delivery of housing target (20,000 homes) Build-to-Rent residential joint ventures to generate capital Build for Sale residential joint ventures to generate capital	Existing secondary residential portfolio with high vacancy rates and significant capex requirements

Sector	Invest/Retain	Rationalise/Divest
Arches	Priority assets and arch runs Place-making enhancements	Review outer London arch portfolio (potential significant capex to meet sustainability requirements)
Offices	Joint venture development portfolio of purpose-built market leading assets Core central London existing office stock	Secondary existing office portfolio with high vacancy rates and significant capex requirement
Car Parks	Green energy initiatives Diversity income – meanwhile uses and environmental enhancements	Redevelopment or disposal of sites with limited value and operational costs
Infrastructure	Bus garages Review value engineering opportunities in existing long leases	Large number of low value non-core assets to be reviewed Review commercially poor performing assets to consider transfer back to TfL as operational assets

- 5.7 The annual valuation reinforces the direction of travel to undertake an optimisation and rationalisation exercise of TTLP's long tail of assets, particularly on the existing retail portfolio and secondary office space.
- 5.8 A comprehensive review of the existing portfolio has been undertaken over the last 12 months with global real estate services provider Savills to identify disposal opportunities. In line with the market, there is a strong case to rationalise TTLP's asset base and the disposals are focused on less-resilient sectors or assets not in the right strategic locations.
- 5.9 Further detail regarding programme and potential receipt levels is set out in the exempt paper on Part 2 of the agenda.

List of appendices to this report:

- Appendix 1: CBRE Monthly Index (March 23)
Appendix 2: CBRE Monthly Yield Index (March 23)

Exempt supplementary information is contained in a paper on Part 2 of the agenda.

List of Background Papers:

TTLP Properties Limited Investment Strategy 23 March 2023

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