APPENDIX B
AGENDA ITEM NO. 5

AYLESBURY VALE ESTATES BUSINESS PLAN 2014-15 Jon McGinty

1 Purpose

1.1 To give the Committee an opportunity to consider a draft Business Plan prepared by Aylesbury Vale Estates LLP (AVE) for the 2013-14 financial year and pass their comments onto Cabinet.

2 Recommendations

2.1 Whether the Committee wishes to make any comments on the draft Business Plans at Appendices 1 & 2 (appendix 2 contains the business plan for the AVE subsidiary company Hale Leys LLP), with supporting documentation in appendices 3-6, for consideration by Cabinet.

3 Supporting information

3.1 As the Committee will be aware, the Council and the Akeman Partnership LLP (Akeman) set up AVE as a Limited Liability Partnership (LLP) in October 2009, following a competitive dialogue procurement, to manage, improve and develop the Council's commercial property portfolio and provide an income stream to the Council. Upon completion of the agreement the Council sold the majority of its industrial and commercial estate to AVE LLP at market value.

3.2 The partnership is governed by a formal Members' Agreement and managed by a partnership board on which the Council has 3 representatives (one AVDC appointment is currently vacant, but this does not affect voting rights as the respective partners vote collectively). Akeman produced a draft Partnership Business Plan for AVE as part of their bid, which was approved by the Cabinet in June 2009. The final version of the Plan formed part of the completion documentation approved in October 2009. The Board meets on a regular basis to review progress on the Business Plan and monitor performance of the Asset Manager, Akeman Asset Management LLP.

3.3 The Members' Agreement provides for AVE to prepare a new Business Plan before the end of their accounting year (which now mirrors the Council's financial year) and circulate this to the Council and Akeman for approval. The Agreement also provides that the Council and Akeman will use all reasonable endeavours to agree the Business Plan within 90 working days. A draft plan was first presented to the Partnership Board at their meeting on 26th March but it was decided by AVDC and also the private sector partners to refine it at subsequent Board meetings and in discussion with AVDC officers and delay submitting it to Akeman and AVDC. A number of iterations followed, and the Board agreed to recommend the attached draft plan for approval at its meeting on 15th August. Following consideration by this Committee the draft Plan, together the Committee's comments will be reported to Cabinet on 4th September.

3.4 The Members' Agreement requires the Business Plan to set out AVE's objectives for the life of the Partnership (i.e.20 years) and the annual overarching objectives for each accounting period. In particular the Plan must include a statement that AVE's business shall be operated with a view to producing the best risk adjusted profit obtainable and to maximise the risk adjusted rate of return to the Council and Akeman. Subject to agreement between AVE, Akeman and the Council the Plan is also expected to include the following matters (based on a 3 year projection where appropriate):-

- Strategic business objectives and targets
- Gross and net rental income projections, including assessment of operating costs, rental voids, rent arrears and any other losses and receipts
- Annual portfolio valuation prepared to a standard acceptable for AVDC financial reporting purposes
- Confirmation that the financial covenants regarding loan to value and interest cover are being maintained
- Projections of estimated receivable rent and confirmation of compliance with maintaining portfolio income levels
- Proposals for working capital budget, any new capital investments and reinvestments plus any distributions to partners
- Performance against key indicators and targets indicate levels of achievement.

3.5 Once approved, the Partnership Business Plan provides the framework within which the Partnership Board works, similar in effect to the Budget and Policy Framework set by Full Council for the Cabinet. Accordingly if the Board wish pursue any substantive action which is not provided for in the Business Plan they must obtain specific authority from the Council (either by a Cabinet or Cabinet member decision) and Akeman. The Committee are therefore invited to consider and comment on the draft Plan.

Index to the Business Plan and Supporting Documentation

3.6 The draft Business Plan, attached as confidential Appendix 1, is accompanied by an Asset Management Strategy for each portfolio asset. The Asset Management Strategy is included as confidential Appendix 3. The draft Business Plan identifies that the 'core assets' within the portfolio - those assets which have the greatest collective bearing on the portfolio in total, and are therefore the subject of greatest management attention - are the estates at Rabans Lane North, Rabans Lane, Stocklake, and Gatehouse Way. For this reason and for the first time in this partnership, these assets have their own dedicated Asset Management Strategy which is attached as confidential Appendix 4.

3.7 During the 2012-13 financial year, AVE purchased the Hale Leys shopping centre, creating a separate special purpose vehicle, Hale Leys LLP, to own and manage the centre. By value, the shopping centre makes up about a quarter of the total portfolio value of AVE, hence it has its own dedicated business plan, attached at confidential Appendix 2.

3.8 The Business Plan necessarily includes a range of assumptions about the future behaviour of tenants and the wider market. Some of these may come to pass, some may not. In order to provide Members with an improved understanding of the impact which these events may have on the performance of the business, two 'cases' have been developed: a pessimistic 'base' case and an optimistic 'enhanced' case. (The expectation is that reality will fall somewhere between these two extremes) A three year ahead budget forecast for each of these cases is attached as confidential Appendices 5 and 6 respectively.

Analysis and summary of key issues in the business plan

3.9 The Business Plan is introduced by a number of key headlines, a number of which are worth repeating in this open covering report:

- The core aims of the company remain the same:

  increased investor revenue flows and

  support for the Council's economic development ambitions.

- After the last few years of rationalisation and stabilisation of the portfolio, through the recession, the focus going forward is now on redevelopment, investment and portfolio growth.
- Consequently, there are no planned asset sales in the new three year plan. However, development sites, which may need to move into joint venture before development commences, appear in the cashflow as a disposal out of AVE.
- New Key Performance Targets have been set for both aggregate rent invoiced and level of void property held highlighting the importance given to these two metrics.

3.10 So this new Business Plan takes the company into a new, and hopefully exciting period, one which is anticipated to be markedly different to the challenging period the company has operated in so far.

3.11 The last few years have been ones where AVE has struggled to keep the levels of voids (vacant properties) to levels as low as would have been desired, due to the depth and length of the recession. They have also been years where AVE has rationalised the portfolio, in part to improve and stabilise the financial position of the company, and in part to create a clearer management attention on the core elements of the portfolio.

3.12 A number of asset sales were implemented in particular in order to create enough cash to pay off the Council's high mezzanine short term loan. This programme of sales of 'non-core' assets has been successful, and AVE anticipates paying this loan back at the earliest opportunity in October 2014. Paying off this loan will be a game changer for the company's cashflows, allowing the company to move from a deficit to a profitable position, and thus able to pay dividends, for the first time in several years. It also allows the company to say in this business plan that no further asset sales are planned over the next three years, other than if development sites come forward to fruition.

3.13 From the Council's perspective, AVE's repayment of the mezzanine loan will generate a sizeable capital receipt but will leave a hole in the Council's revenue budget in the short term, as the loan repayments would cease in October 2014. However, the benefits accruing to AVE's cashflow will grow gradually thereafter and over time should allow the company to reward AVDC and other investors with rental and dividend income to replace loan income.

3.14 The enhanced case proposed in the business plan also discusses potential ways in which the Council can mitigate the short-term revenue impact of the mezzanine loan repayment stopping, for instance by considering amortisation holidays on the senior debt, or by offering AVE new commercial loans for new acquisitions. Any such move by the Council would need to be properly evaluated and the necessary approval sought.

3.15 Reducing the level of voids is also a priority for the company going forward. Finding tenants has a positive 'double-whammy' effect on the company's cashflow: not only does rental income increase, but liabilities for empty property business rates decreases.

3.16 To this end, AVDC and the private shareholders have held extensive talks with Akeman Asset Management over the development of a new Key Performance Target (KPT) for the asset managers to achieve, and ways in which this level of performance can be delivered (for instance through broadband initiatives and new marketing activity). The shareholders' view, which the asset managers regard as achievable, is that the level of voids should not exceed, and ideally should be below, the regional average for similar industrial units, within two years. The business plan therefore sets out a new KPT for the asset managers based on these numbers, with interim targets for each year of the plan.

3.17 In order to avoid creating a perverse incentive with this KPT (i.e. AVE could simply sell off empty units to achieve the goal), a second KPT has been agreed, which directs AVE to increase the amount of rent billed, year on year.

3.18 There remain a number of significant asset management challenges for AVE on the horizon. In particular, a number of major tenants have lease breaks or expiries in the next two years, which they may choose to exercise (this explains, in part, the scale of the difference between the base and enhanced cases presented in the business plan). AVE has to plan for such scenarios. These issues are discussed in paragraphs 4.11-4.13 of the business plan, as well as in the various supporting asset management strategy documents.

4 Resource implications

4.1 Cashflow analysis, supporting both the base and enhanced cases set out in the business plan, are provided in confidential appendices 5 and 6 respectively.

4.2 Since its creation AVE has struggled to deliver against its Business Plan cashflow projections. The reasons for this have previously been extensively reported in the Council's budget planning processes and in previous AVE monitoring reports. In summary this has been attributed to the national economic conditions which have prevailed since AVE's creation, compounded by the legislative changes to Business Rates.

4.3 AVE's business case was, by necessity, always saddled with a high level of debt in its early years. This was necessary in order to produce the return which the Council required. However, the unprecedented length and depth of the economic malaise which the Country has experienced over the past 5 years came at exactly the wrong time in the business plan cycle, and impacted during a period where AVE was least able to deal with it.

4.4 During the past 5 years, it has managed to maintain its interest repayments to the Council, (the largest element of its financial commitment), and acquired ownership of some new assets, including Hale Leys, but has not managed to grow its income sufficiently to be able to pay dividends.

4.5 Over the past few years it has therefore focused on the restructuring of the estate by disposing of underperforming assets in order to put it in a position of being able to reduce its debt gearing this October. This will give AVE the headroom it needs to re-invest and grow income and dividends in line with its original objectives. With signs that the economy is now finally growing again, this should ensure that AVE is well placed to capitalise on the improving position. The Business Plan has been expanded at the request of the investors to set out how this will be achieved and the plans for individual assets.

4.6 The satisfaction of existing tenants is also an important consideration as AVE's success depends on maximising the income from its existing estate through high occupancy levels. Only by satisfying the needs of tenants can this be achieved.   From an investor perspective, it was felt that insufficient focus was being given to this, hence the introduction of a new key performance target. This should ensure that equal focus is given to managing existing business relationships as is given to new investment and growth.

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Background Documents	None