Corporate Estate Annual Report

for the Year Ended March 2024

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1. FOREWORD FROM THE DIRECTOR

Welcome to Leicester City Council's Corporate Estate Annual Report for the year ended March 2024.

In closing the financial year, we present resilient results against a backdrop of a challenging market and UK economy.

Citing the RICS's economic outlook report for 23/24, the UK Economy's overall momentum was at best 'sluggish' last year. The two quarters ending the year saw the UK economy slip into a mild recession, feeling the impact of the steepest rise in policy interest rates set by the Bank of England over a two-year period since the late 1990s. This, coupled with the cost-of-living crisis and a Consumer Price growth averaging 7.4% for 2023, this has been felt across commercial tenants' and households' finances, individually and collectively.

In many ways our commercial real estate portfolio performance in 23/24 echoes that of the wider sentiment of market analysts, indeed it demonstrates stoic and resilient performance, producing a gross yield of 7.66%, an improvement on last year and a very good result when compared to the national benchmarks. Managing the pressure around operational running costs and the impact on our tenants has been driven by higher utility and maintenance/construction costs. The post-pandemic market continued to bite particularly in the secondary office and retail sectors.

The overall valuation of our portfolio has seen a slight contraction, down by 2% to £147m for 23/24. Over and above the UK real estate market stagnation, strategic disposals of assets being the main reason for this change. At £11.27m our gross rental income has held its ground well, albeit being a touch down at £190k (1.65%) from last year. The successful launch of a focussed lease review programme has enabled us to engage more closely and meaningfully with our occupiers, tenants and their customers, to support them with refreshed and more flexible terms and arrangements. This has also supported improved service charge management and recovery. The upsurge in global utility costs (gas/electric) alongside increasing repairs and maintenance costs, (particularly around some of the ageing assets in our estate) have resulted in operational management and running costs increasing and a credible net income of £5.68m, albeit down from last year. Bad debt has been driven down from £3.2m to £0.9m. With no significant issues in occupancy levels at 95.5%; availability is 4.5% and the portfolio remains well-let. Investments into new light industrial and workspace will greatly help us as a city as demand levels continue to be high.

The Council's Corporate Estate portfolio has been built over many decades of investment, it's fair to say that we are in it for the long-haul. We will continue to invest and dis-invest locally, pro-actively managing our portfolio purposefully, yet empathetically, to ensure we are doing what we can to support our tenants and the long-term economic prosperity of Leicester — operating our portfolio commercially, in line with the prevailing markets, yet with an embedded Environmental, Social, and strong Governance (ESG) reducing carbon in our buildings to meet our net zero targets. With our emerging Heart of Leicester Strategy, and working together, the city's future remains bright, and we will continue to ride market storms.

Matthew Wallace BSc (Hons), MBA, DipProjMan, FRICS
Director of Estates and Building Services

2. Background to the Council's Land and Property Holdings

Leicester City council holds a diverse portfolio of land and property assets ranging from historic buildings such as the 13th century Guildhall to the more recent strategic investments for The Corporate Estate of the Haymarket Shopping Centre in 2019/20 and The Heathers Industrial Estate in 2023/24. For the most-part, however, the wider estate owned by the council is held and managed in order to provide front line services for the city's residents in the form of homes, schools, leisure centres, and neighbourhood centres as well as Green Flag parks, playgrounds and open spaces providing areas for leisure and recreation. There is also critical infrastructure such as bridges, footpaths, cycle paths and car parks that aid the smooth running of the city.

The grouping of land and property assets, known as The Corporate Estate, is held for commercial reasons. It is the council's investment portfolio that is managed in-house, and provides local businesses with commercial premises, offices, shops, industrial units, and workspaces for new business start-ups, which generates an income for the council that is used to re-invest in its services.

The Council's Property Holdings

HOLDING	DETAILS
The Operational Estate	The land and property held to support the main business of the Council, including: • property utilised for the provision of front-line services to the public such as museums, libraries, leisure centres, and neighbourhood centres; • playgrounds, parks and open spaces; • property leased to community groups and charities; • property occupied by council staff in order to support delivery of council services – such as City Hall, Town Hall and council depots; • cultural, historical and heritage assets.
Schools	Includes both community and maintained schools as well as academy schools.
Housing	The council's housing stock.
Highways	Includes roads, footpaths and bridges as well as land and buildings that may be required for future transport development schemes.
Strategic/Regeneration	Property and land acquired for strategic purposes, to promote regeneration and redevelopment of the city.
The Corporate Estate	The land and properties held by the council for income generation which supports general Council services, rather than to provide accommodation for the council or direct services to the communities. Provides a wide range of accommodation for local businesses.

This annual report focusses on the performance of The Corporate Estate for the financial year from 1 April 2023 to 31 March 2024.

The Corporate Estate — A Long-Term Investment

Leicester City Council has been investing in land and property for generations, enabled by the special powers afforded through parliament, including the 1956 Leicester Corporation Act that gave the Leicester Corporation the powers to buy, sell and manage land and property for highways, education, planning and investment purposes, and more recently — in terms of holding and managing land and property for investment purposes — the Local Government Act 1972.

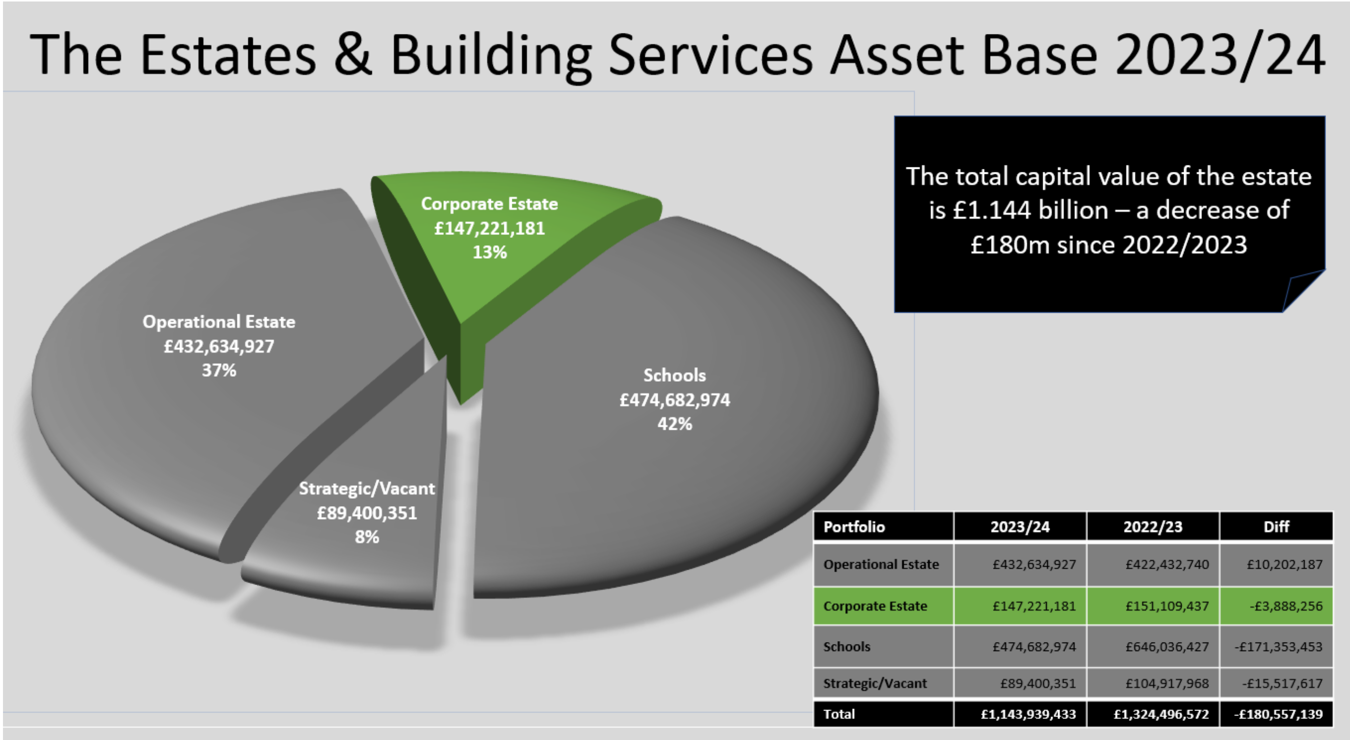
The council's Corporate Estate, and our investment in and management of land and property, has benefited from our successful long-term strategic planning of the portfolio. As opposed to other local authorities that in recent years have been taking significant risk when it comes to their investment in property and continue to be reliant on their investments to shore up gaps in their budgets.

Whilst other investors are significantly influenced by how the market is performing at any given time, as a public body we are able to take a long-term view of the needs of the city — something that other investors are not always able to consider. The benefits we receive today, in terms of a growth in value and income to the council, along with our ability to bring forward land for redevelopment, are a direct result of the prudent investment and wise management of The Corporate Estate portfolio throughout the years.

Our FY 2023/24 report demonstrates clearly why our long-term views, and balanced approach are working well and will continue to do so in the years to come.

The Corporate Estate — the council's investment portfolio — is a small part of a broad range of Leicester City Council land and property holdings, making up 13% of the overall capital asset valuation* of the Estates & Building Services estate (excluding housing and highways).

CHART 1 – ESTATES AND BUILDING SERVICES ASSET BASE



Portfolio	2023/24	2022/23	Diff
Operational Estate	£432,634,927	£422,432,740	£10,202,187
Corporate Estate	£147,221,181	£151,109,437	-£3,888,256
Schools	£474,682,974	£646,036,427	-£171,353,453
Strategic/Vacant	£89,400,351	£104,917,968	-£15,517,617
Total	£1,143,939,433	£1,324,496,572	-£180,557,139

The Estates & Building Services (EBS) capital asset base is valued at £1.144bn in 2023/24 (this includes: Schools (42%), Operational (37%), Corporate Estate (13%), Regeneration (8%)). The EBS capital asset base excludes Highways and Public Realm (£1.8bn) and Housing (£1.2bn).

** The FY23/24 Annual Audit of Assets is in progress and will complete in October 2024. For the purpose of this report, the figures contained within for valuation will not be formally signed off until reported to Governance & Audit Committee in November 2024, therefore all figures and assumptions are subject to audit.*

Economic Regeneration Workspaces

The land and property in The Corporate Estate portfolio is held for investment purposes, e.g. for the benefit of the city and the generation of ongoing revenue income to support Council services. There are also council managed workspaces that sit outside of The Corporate Estate portfolio that are held for economic regeneration purposes and let out to local businesses. Whilst both portfolios generate revenue income to invest back into council services, and both benefit from high occupancy and strong demand, it is useful to understand the difference between the two portfolios in terms of their aims.

The economic regeneration workspace portfolio focuses primarily on supporting the growth of priority economic sectors with the service directly managing six workspaces: LCB Depot, Makers Yard, Phoenix Square Workspace, Dock, Dock 2 and Gresham Works. This provides a total of 90,000 sq ft lettable space for local small businesses. Two workspaces with outsourced management via East Midlands Chamber — Leicester Food Park and Friars Mill — provide a further 36,500 sq ft of lettable space. Several new workspaces are in development, including three further Dock workspaces which opened in September 2024, and Pilot House due to open in Summer 2025.

These workspaces are effective in delivering the following:

• Helping to reposition Leicester’s economy to grow knowledge-based sectors, including creative industries and innovation/technology businesses.

• Significant job creation performance, supporting over 800 jobs in tenant businesses, rising to over 1,100 jobs with the delivery of the new schemes when they ultimately reach full occupancy.

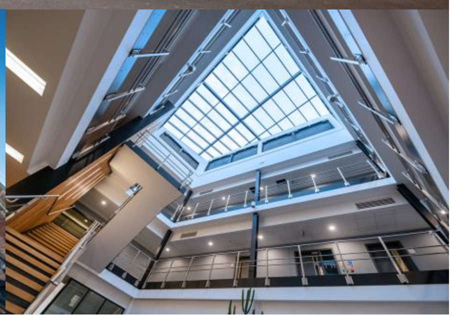
• Providing a physical focus for clustering, networking, and collaborative working — there is evidence that this increases the survival rate for small businesses who are tenants. For example, the

LCB Depot has been driving the delivery of Design Season over recent years, an annual showcase for the city's design strengths.

Workspaces have proved an effective mechanism to kick start the delivery of regeneration areas, particularly through raising investor confidence and ultimately stimulating other private sector investment. This has been the case with St George's Cultural Quarter, Pioneer Park/Space City and Waterside, where workspaces have been the first key regeneration intervention.

The Corporate Estate on the other hand consists of a diverse portfolio with a range of long- and short-term leases in order to balance out risk. It is managed as a commercial operation whilst making a significant contribution to the council's commitment to support the local economy, maintaining a retail presence in the city centre and neighbourhoods, and supporting local businesses by providing a range of accommodation with space for new business start-up to grow on locally, maintaining good employment prospects in the city.

The largest single sector portfolio in terms of numbers is the office portfolio with 425 lettable units, whilst the four managed workspace buildings house more than 250 lettable units. There are 374 industrial units and almost 300 retail units — more than a third of which are neighbourhood shops. The Corporate Estate all sectors have remained reasonably static year-on-year. There are a further 165 'other' assets that are neither office, industrial nor retail sectors which includes assets such as agricultural holdings.



3. Executive Summary

The commercial property market in the UK is well-established and, despite the commercial real estate market experiencing a steep drop in buyer activity in FY2023/24, recent market reports suggest it is expected to recover modestly in FY2024/25 albeit with some variation by sector. The downward shift in interest rates in August 24 is expected to improve investment opportunities from a wide range of investors including local authorities, pension funds, and high net-worth individuals in FY24/25.

The market offers a wide spread of yields that are influenced by both the quality of the assets (e.g., location, sector, condition, supply, and demand) as well as the associated investment risk. A low-risk investment for example would be well-located and leased at a market rent to financially stable tenants on a lease that has more than 10 years until expiry. Whilst net yield is important in determining the actual profitable return achieved, running costs can fluctuate dependent on how efficiently land and property is managed. As a result, gross yield is generally used to compare the financial performance of property investments. 5-6% is considered 'good' rental yield with above 6% being considered 'very good'. This years' results of 7.66% gross yield demonstrates that the council's commercial real estate holdings are considered 'very good' against a difficult UK financial backdrop.

The Corporate Estate is a long-term investment portfolio consisting of the land and property held and directly managed by Leicester City Council predominantly for income generation to support wider Council services and for the most-part, let out at market (or market-competitive) rates.

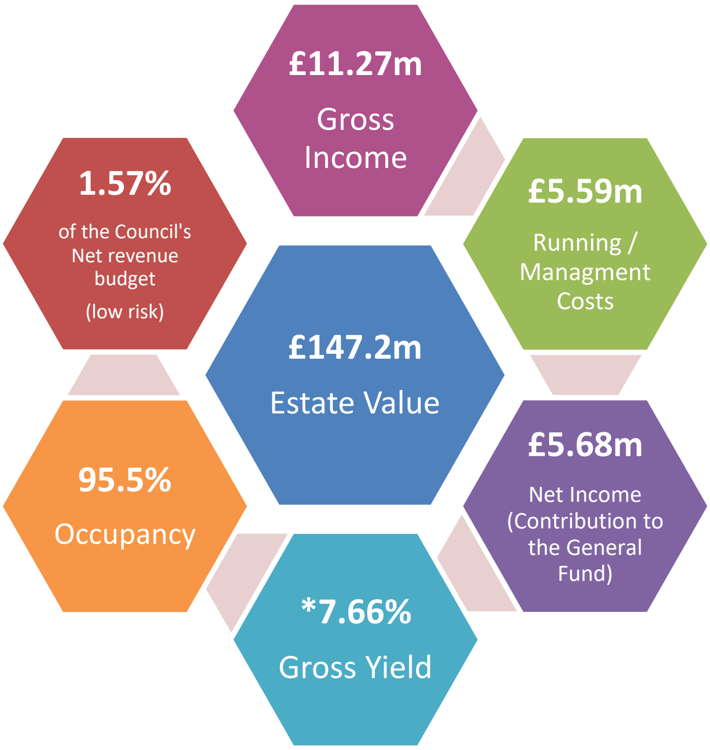
The portfolio is extremely broad and well-balanced — consisting of land, small business units, office space, car parks, industrial units, and city centre retail units/neighbourhood shops that are leased out to private sector organisations across the city. In addition, the council leases out a significant amount of land that houses a variety of properties — from warehouses and factories to sports facilities and sub-stations — as well as agricultural holdings such as farms and grazing land.

The corporate estate:

- Continues to generate a stable and sustainable revenue income contribution for the council — providing market-competitive returns. Key economic factors such as inflation and utility costs have impacted net income in FY23/24, however yields are strong and above benchmark averages.
- Is a diverse portfolio — in line with the council's investment strategy that requires a balance of security, liquidity, and yield to minimise risk.
- Certain assets require significant capital investment in order to maintain overall asset values; necessary investment in repairs and maintenance has impacted running costs.
- Is wholly invested in our local economic area (Leicester and Leicestershire).
- Includes land and property that is held for economic regeneration purposes (although the capital values are included in this report, income from these investments is not included as the properties are managed separately).
- With a GIA (floor space) accounting for 17% of the council's estate holdings*, has a continued and significant role to play in our commitment to address the climate emergency.
- Supports the local economy and local businesses by providing a range of competitively priced accommodation.

*Excludes Housing, Highways and the council's investment in pooled property funds that are governed by Treasury Management.

Summary of Performance for the Year Ended 31 March 2024



*Denotes very good performance against gross yield Benchmarks

Yield Benchmarks used:

- **CCLA Local Authorities' Property Fund** gross yield 4.84% (Annual Report FY2023/24). Down -13.17% on FY22/23

Key Performance Factors	2023/2024	2022/2023	2021/2022	2020/2021
Value of the Corporate Estate	£147,221,180	£151,109,437	£123,031,773	£112,287,183
Gross Income	£11,270,686	£11,462,492	£8,337,033	£7,484,007
Running / Management Costs	£5,593,788	£4,991,567	£2,479,083	£2,138,819
Net Income (contribution to the General Fund)	£5,676,898	£6,470,925	£5,857,950	£5,345,188
Net Yield	3.86%	4.28%	4.76%	4.76%
Gross Yield	7.66%	7.59%	6.78%	6.67%
Occupancy	95.50%	96%	95%	95.50%
% of the Council's Net revenue Budget	1.57%	2.02%	2.03%	1.92%

4. Understanding Our Corporate Estate in FY2023/24

Portfolio Key Facts

375 Sites
(including land)

1,263 Lettable Units
(including land)

£147.2m
Valuation* at 31 March 2024

1.63m sq ft
Total Gross Internal Area (GIA (floor space))

Accounts for 17% of the total GIA
(floor space) of the estate owned by the council

120.2 Hectares
(excluding farm and agricultural land)

£414,140 p/a Largest single rent
(3.67% of gross rent)

The Industrial Sector continues to be the largest single sector by GIA and value

** The FY23/24 Annual Audit of Assets is in progress and will complete in October 2024. For the purpose of this report, the figures contained within for valuation will not be formally signed off until reported to Governance & Audit Committee in November 2024, therefore all figures and assumptions are subject to audit.*

Scope of the Estate

The Corporate Estate property portfolio provides a broad range of commercial space across the traditional office, retail, and industrial sectors, as well as a significant offering in terms of other less traditional space for rent - including advertising hoardings, substations, grazing land, farms, garages, and car parks.

The chart below shows that, in terms of actual sites, the Council holds 59% of its investment holdings in the industrial, retail and office sectors with the other 41% being a wide spread of other land and property (including a number of ground leases and long leases, land, car parks, substations and communication masts, as well as farmland and a handful of residential property (temporarily let while held for re-development purposes)).

CHART 2 – CORPORATE ESTATES SITES

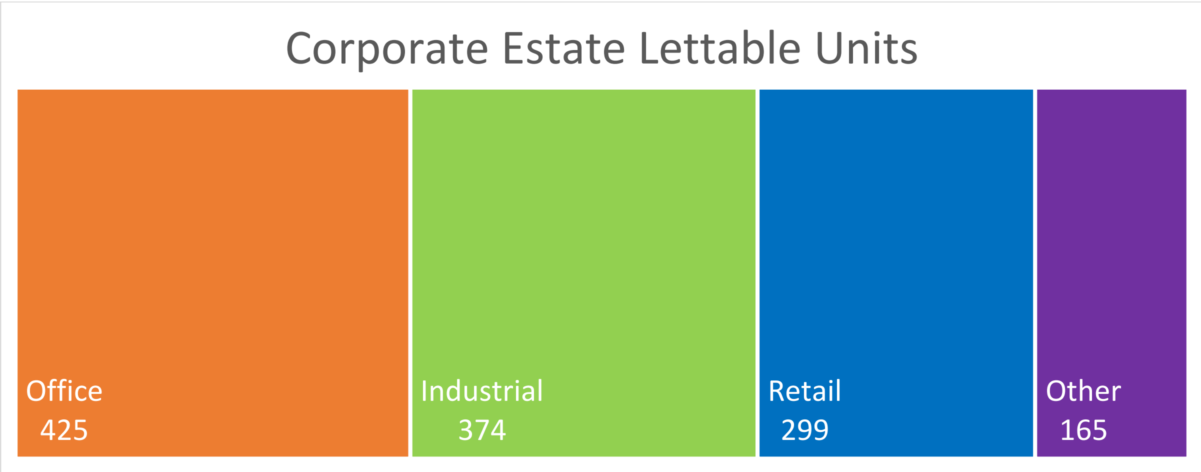
Sites

Sector	Sites
Industrial	109
Office	39
Retail	73
Other	155
Total	**375**

The classification of the estate looks different when we look at lettable units rather than sites. The broad range of assets held in the portfolio, including land that is let on long-term ground leases, provides the council with a low-risk investment return.

As shown in the chart below, the largest single portfolio held by the council for investment purposes is the secondary office market portfolio with 425 lettable units – representing 34% of our available units.

CHART 3 – CORPORATE ESTATE LETTABLE UNITS



Sector	Lettable Units
Industrial (30%)	374
Office (34%)	425
Retail (23%)	299
Other (13%)	165
Total	**1,263**

Compared side by side with the CCLA Local Authorities' Annual Report for FY23/24 we can see in the Chart below, that there is a shift in sector comparators towards Industrial sector investment and away from Office investment with retail investment being reasonably static against last year.

Industrial units make up 44.55% of the CCLA portfolio as compared to 30% of The Corporate Estate. The council have similarly made significant capital investment in industrial sector growth for future years to develop new industrial sites in the future – which will increase this investment figure over the next two years. Sites such as the Former Ian Marlow Centre on Blackbird Road are anticipated to complete in October 2024 and will support ESG through green leases.

The Office sector makes up 18.7% of the CCLA portfolio compared to 34% in The Corporate Estate. The significant difference here is the movement of Grade B/secondary operational offices into The Corporate Estate for letting into the office market. This has proved difficult to let post-covid, due to market requirements for Grade A offices, smaller office footprints, with ESG being at the forefront of requirements with net zero carbon buildings being in highest demand. However, the market is showing a slight upturn in Grade B office interest locally especially for training and education and some government office purposes. In line with the local market, the council's strategy remains firm in ensuring that our office stock is asset reviewed with a priority focus on disposal to the HRA for Housing re-development wherever possible and with meeting the highest EPC ratings. There is a market shift in an increase in the return to the workplace, with most companies now insisting on a minimum presence in the office of 2-3 working days (driven largely by efficiency, mental health impacts, and team-building contact for junior members of staff/apprentices/new employees and graduates).

Investment in the Retail sector by the CCLA's fund of 18.34% compares to 23% in The Corporate Estate with the CCLA's main retail investment in large out of town retail warehousing nationally compared to the predominantly local retail and neighbourhood retail shops within the council's investment portfolio. The investment in the Haymarket Shopping Centre continues to have a positive full-year impact on net income in FY23/24 and capital asset value.

This emphasises the fact that, whilst our portfolio remains reasonably well-balanced across all categories, the council's investment in the Retail sector is not purely for income generation. The council continues to hold and invest in our Retail portfolio for strategic purposes and to support the local economy by providing a range of accommodation for our city centre and neighbourhoods.

CCLA ASSET ALLOCATION – FY23/24 COMPARED TO THE CORPORATE ESTATE FY23/24

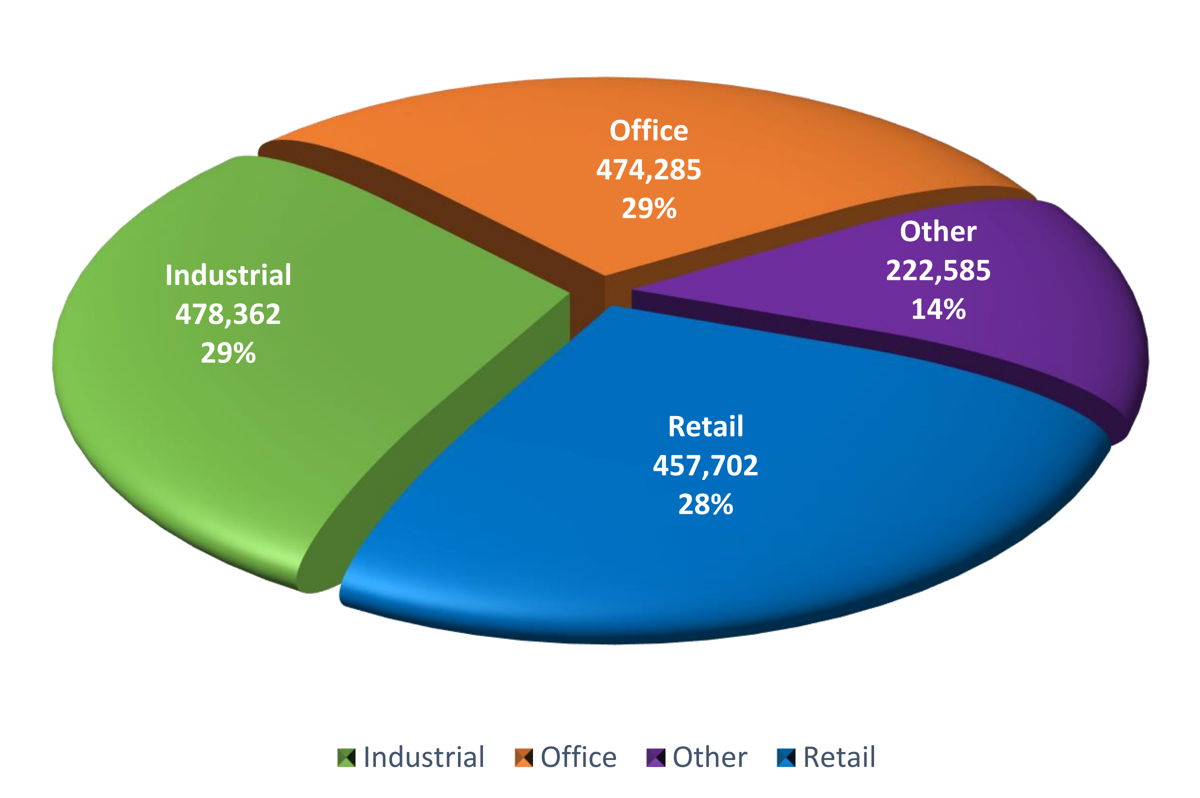
CCLA		**LCC CORPORATE ESTATE**	
Industrial	44.55%	Industrial	30%
Office	18.71%	Office	34%
Retail Warehousing	16.47%		
Retail	1.87%	Retail	23%
Other	18.4%	Other	13%

We have continued to support local businesses by maintaining a sizeable Retail portfolio consisting of city centre retail, neighbourhood shops, and other retail spaces at competitive rents. Alongside this we continue to offer a considerable portfolio of secondary Office space and managed workspaces to our existing city-wide portfolio that offers around 250 lettable units comprising predominantly small office and workshop/industrial units.

Additionally, the council's strategy continues to include a growing number of prime Economic Regeneration workspaces in the city which can compete with the secondary market offering.

Central government's Minimum Energy Efficiency Standards (MEES) Legislation came into force with effect from 1 April 2023. The aim of MEES regulation for commercial property is to help meet the UK government's target to reduce emissions to net zero by 2050. Announcements by the outgoing government in FY23/24 suggested a 'softening' of the legislation, however, this has not been defined. With a new incoming government, it will be interesting to monitor whether stringent legislation will impact the investment portfolio. A minimum EPC rating of E for all commercial real estate lettings, requires that the council continue to review and invest, where economically viable, in the improved sustainability of the Corporate Estate portfolio and older Regeneration units to maintain capital asset values and the ability to continue to lease older properties. Whilst all properties meet the current MEES legislation, the EPC rating becomes more challenging to meet by 2027 when the minimum EPC rating increases to C and by 2030, B.

CHART 4 — GIA BY ASSET CATEGORY (SQ FT)



Retail = 457,702 (down slightly from 466,001 LY)
Office = 474,285 (up slightly from 454,264 LY)
Industrial = 478,362 (no movement from 478,362 LY)

Other = 222,585 (down slightly from 217,849 LY)

Chart 4, above, shows the lettable floor space available and, like the rest the report, is categorised using the traditional sectors of Office, Retail, Industrial and Other. In terms of floor space, 86% of the space on offer is Industrial, Retail and Office (static against last year, but slightly up in office and slightly down in retail exposure). 57% of floor space offered by our retail sector and industrial sector portfolios which is reasonably static against last year. Office space has increased slightly by 20,021 sq. ft due to additional office space from the operational estate moving over into The Corporate Estate as a result of hybrid working. Available space has increased overall by 16,458 sq ft predominantly due to increased office space.

CHART 5 — GIA BY ASSET CATEGORY (SQ FT)

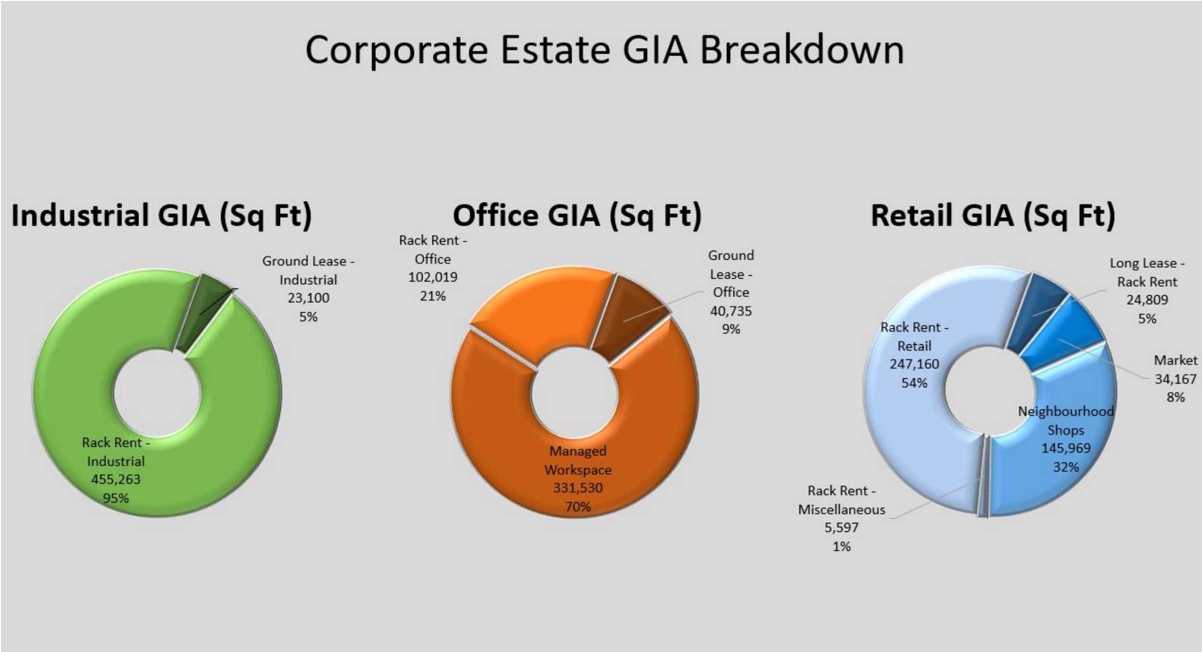
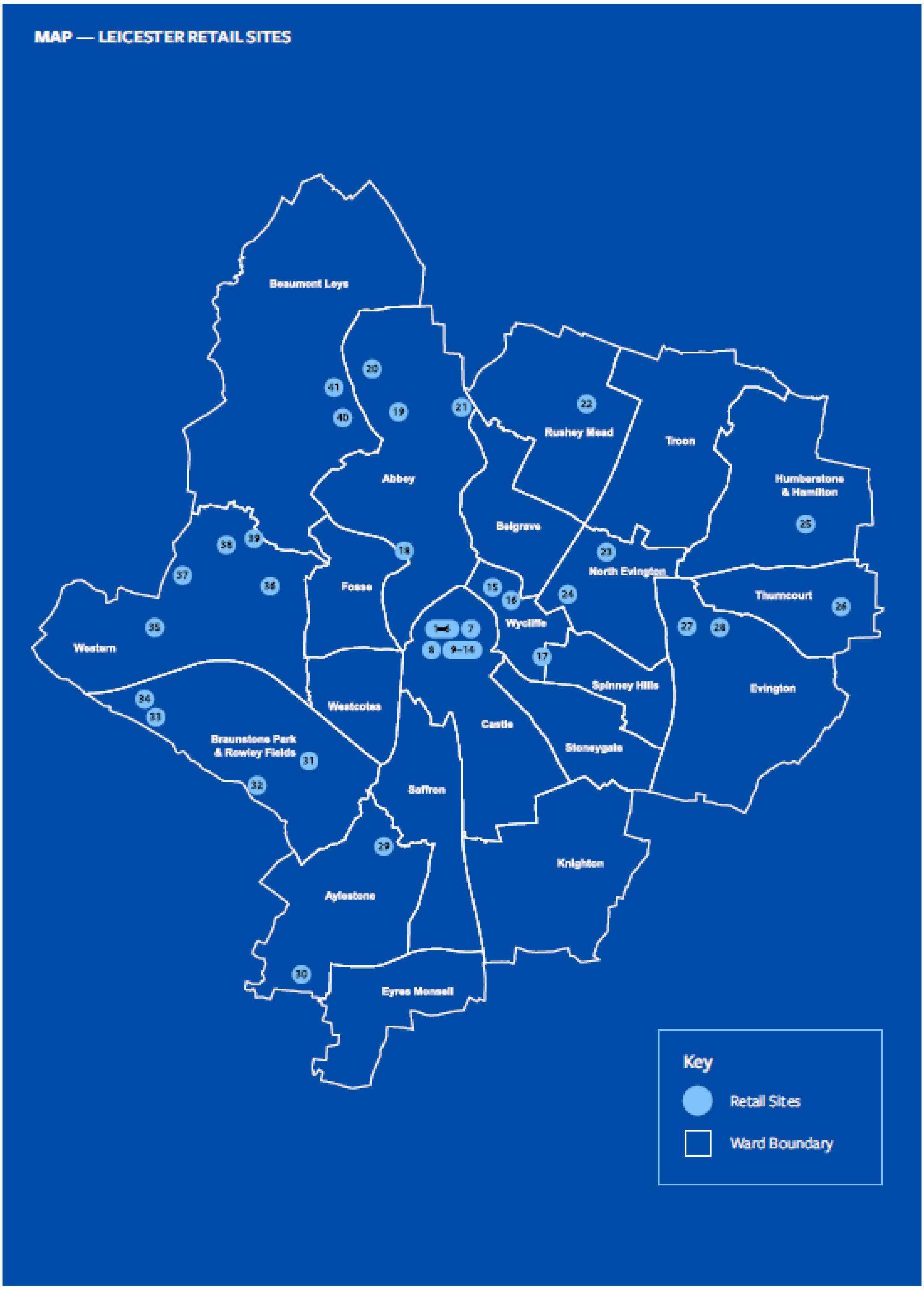


Chart 5a INDUSTRIAL: (left, above) Illustrates the breakdown of the Industrial portfolio across the estate —which represents 29% of the lettable space. The council's estate is almost wholly 'rack rented' or units on long term leases. Long term leases, along with the ground leases, require little support and provide good security of tenure.

Chart 5b OFFICE: (middle, above) Illustrates the makeup of the floor area of our rented office space — which is 29% of our whole estate. With a focus on new business growth, a growing proportion of our office estate is attributable to managed workspace units (70%). Rack rent makes up 21% of the available office space whilst normally this would be growing in the office sector for onward business growth, the market demand has slowed for office space and particularly Grade B office space – this is reflected here. Ground rents are static between last year to this year at 9%.

Chart 5c RETAIL: (right, above) Making up 28% of our overall corporate estate floor space, the chart shows the dispersed nature of our retail space across the city, with 32% of our shop units located within local communities. Our city centre retail estate — including the market — remains significant in the City, and accounts for almost two thirds of the space on offer, with over 457,702 sq ft of retail units available across the city. The diverse spread of locations also spreads risk and places the council in a strong position during financial or market uncertainty.


MAP — LEICESTER RETAIL SITES
Beaumont Leys
Abbey
Rushey Mead
Troon
Humberstone
& Hamilton
Belgrave
North Evington
Thurncourt
Fosse
Wycliffe
Western
Spinney Hills
Evington
Westcotes
Castle
Braunstone Park
& Rowley Fields
Stoneygate
Saffron
Knighton
Aylestone
Eyres Monsell
1–6
7
8
9–14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29
30
31
32
33
34
35
36
37
38
39
40
41
Key
Retail Sites
Ward Boundary

Castle

1. High Street 16 & 16 1/2
   High Street 27
   High Street 29
   High Street 40–50
2. Royal Arcade Shops
3. Malcolm Arcade 1–23
4. Silver Street 14–20
   Silver Street 29–31
   Silver Street 33
   Silver Street 35
   Silver Street 37
   Silver Street 37a–39–41
5. Cank Street 17a–17b
6. Cheapside Kiosk 1 & 2
7. Haymarket House
   — Travelodge Hotel
   Haymarket Shopping Centre
8. Loseby Lane 1
   Loseby Lane 11
   Loseby Lane 13
   Loseby Lane 15
   Loseby Lane 17
   Loseby Lane 3
   Loseby Lane 5–7
   Loseby Lane 9
   Loseby Lane 9a
9. Leicester Market — Retail Units
   Leicester Market Food Hall
   Leicester Outdoor Market and
   Green Dragon Square
10. Horsefair Street 11
    Horsefair Street 23
    Horsefair Street 25–29
11. Corn Exchange
12. Charles Street Retail Units
13. Halford Street 5
14. Granby Street 15–17 — Rear of
    7–9 Every Street

Wycliffe

15. Manitoba Road 82
    Manitoba Road 84
    Manitoba Road 86
    Manitoba Road 88
16. Malabar Road 22–46
    Malabar Road 26
    Malabar Road 34–38
    Malabar Road 48–50
17. Melbourne Road 100–114

Abbey

18. St Margarets Way 80
19. Marwood Road 8–20
    (No 10 not included)
20. Bewcastle Grove 12–22
21. Abbey Lane/Red Hill Circle

Rushey Mead

22. Lockerbie Walk 1–6

North Evington

23. Hastings Road 80–86
24. Charnwood Walk 5–11

Humberstone & Hamilton

25. Netherhall Road 83–119

Thurncourt

26. Thurncourt Road 166–200

Evington

27. Radstone Walk 35–41
28. Rowlatts Hill Road Supermarket

Aylestone

29. Aylestone Road 473
30. Hopyard Close 1–5

Braunstone Park & Rowley Fields

31. Fosse Road South 300
32. Hallam Crescent East 170
33. Cantrell Road 29
    Cantrell Road 7
    Cantrell Road 9
34. Heyford Road 69–71
    Heyford Road 73–75

Western

35. Sharmon Crescent 29–39
36. Aikman Avenue 120
37. Musson Road 6
38. Aikman Avenue 277–311
39. Bonney Road 56

Beaumont Leys

40. Home Farm Close Supermarket
    Home Farm Square 1, 5–8
    Home Farm Square 2–4
41. Cross Hedge Close 11

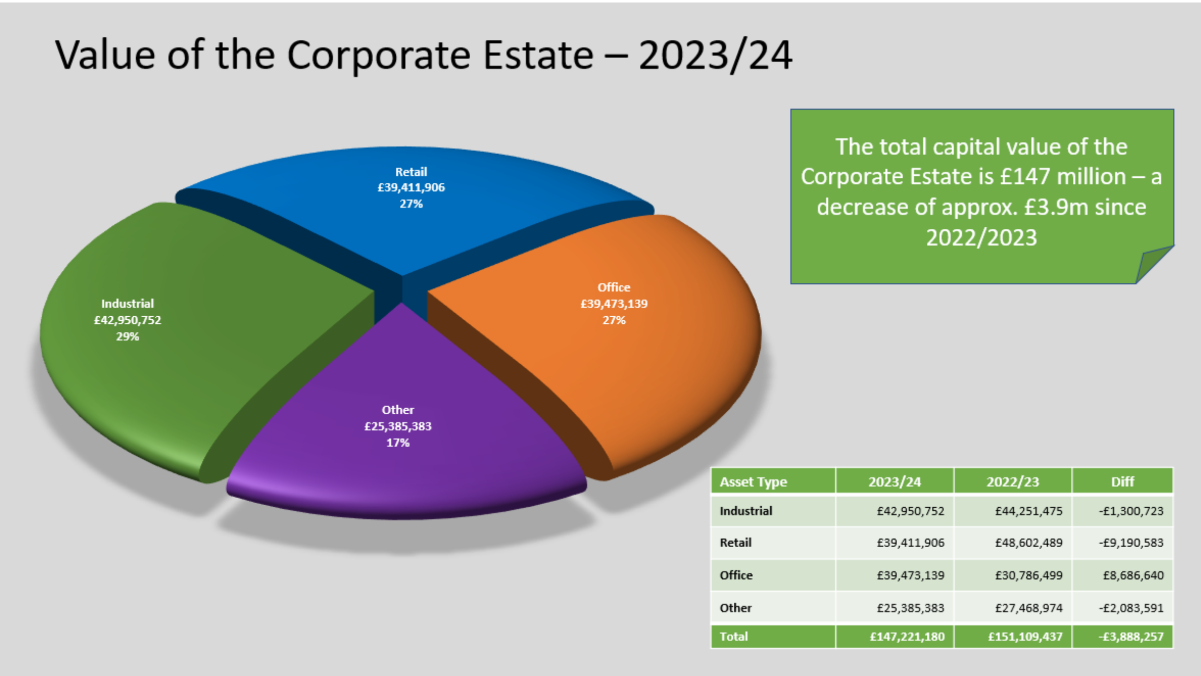
5. VALUATION

The valuation methodology has been brought in line with the RICS Code of Practice for the Commercial Property Sector and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom with effect from 1 April 2023, where 20% of the Council's real estate portfolio was re-valued and the remaining 80% were valued through applying a 4% RPI indexation.

This change in valuation methodology combined with market impacts has resulted in a reduction in the valuation of the Council's commercial real estate portfolio of £3.9m, from £151.1m in FY 2022/23 to £147.2m in 23/24.

The Corporate Estate represents 13% of the EBS £1.144 billion valued assets in FY 2023/24. The Corporate Estate Portfolio comprises traditional sectors of Industrial, Office, Retail and Other.

CHART 6 – VALUE OF THE CORPORATE ESTATE – FY2023/24



Asset Type	2023/24	2022/23	Diff
Industrial	£42,950,752	£44,251,475	-£1,300,723
Retail	£39,411,906	£48,602,489	-£9,190,583
Office	£39,473,139	£30,786,499	£8,686,640
Other	£25,385,383	£27,468,974	-£2,083,591
Total	£147,221,180	£151,109,437	-£3,888,257

Turning our attention to wider UK market, the RICS Modus Property Journal reported that all three mainstream sectors of the commercial property market suffered steep declines in buyer activity in FY23/24 compared to FY22/23. Retail volumes were down by around 30%, while office and industrial investment both slumped by around 50%.

Alongside the drop-off in activity levels, capital values also fell noticeably in FY23/24, with month-on-month declines being recorded throughout the entirety of the second half of last year – slipping by a total of 3.5% across all sectors. Compares to Leicester's capital value decrease of 2.65%.

This brought the cumulative decline in headline values since mid-2022 to 22%, according to CBRE. That said, not all mainstream sectors saw valuations retreat further during FY23/24, with the industrial sector posting a small recovery of 1.4%. However, this followed what had been a sharp fall of 21% during the prior year.

Meanwhile, across the retail sector in aggregate, capital values slipped by a further 4.2% last year, extending on a decline of 8% registered the year before.

The largest decline in values, however, came in the Office sector, which chalked up an 11.5% drop over FY23/24 following a 12% decline FY22/23.

These unquestionably weak trends are also reflected in the share prices of many real-estate investment trusts, with British Land and Land Securities down by a respective 30% and 15% compared to FY22/23.

Headline capital values – while potentially coming under some further downward pressure over the first half of FY23/24 – are anticipated to stabilise inFY24/25. The net balance for the 12-month capital value expectations, taken from the RICS UK Commercial Property Monitor, stands at just -7% across all sectors. This reading should be interpreted as respondents envisaging a virtually flat outturn for the year to come.

Changes to The Corporate Estate's valuation in FY23/24 focuses on the following:

Leicester City Council's Corporate Estate's Market is secondary in nature, and it is similar to the other East Midlands cities in that regard. Looking at the Leicester and Leicestershire market in FY23/24, the trends listed below emerged:

- Industrial Annual rent growth has decelerated since last year to today's rent amid a cooldown in tenant demand and rising vacancy.
- Office rents remained stable at 2022 levels, with prime values at £20 per sq ft and secondary rents at £14 per sq ft. Comparables sought from CoStar indicated the prime office rents in the city centre are £20 per sq ft, while secondary rental values are around £14 per sq ft, excluding incentives.
- Retail Asking Rent in the city centre is around £25 per sq ft, with vacancy rate in the region of 389,234 sq ft which equates 3.6% of the market.

Take-up in the Leicester Office market moved back above the 10-year average in FY23/24, with total activity of 366,740 sq ft. Sales and lettings were primarily focused on better quality second hand space, with two-thirds of activity out of town.

The largest letting was at Granite House on Watermead Business Park, Thurmaston, where E.ON took 24,863 sq ft. The largest transaction in the city centre to an occupier was the freehold purchase of Bankfield House on New Walk, by Planet Education Networks of 14,554 sq ft.

Supply tightened in FY23/24, falling to 805,322 sq ft, with the focus being on second hand space, which accounted for 93% of stock on the market. Grade A supply overall stood at 90,840 sq ft and is primarily focused out of town at Carlton Park, Narborough. Supply within the city centre was as low as 16,200 sq ft.

Considering the Industrial sector, the take-up in the Leicester industrial market remained above the 10-year average for the fourth successive year in FY23/24, with total activity of 2.7m sq ft. The 'Big Box' market continued to see good levels of activity, with six deals totalling 1.25m sq ft.

The largest deal was the 493,000 sq ft build for Persimmon's timber frame manufacturing subsidiary Spring 4, at Garendon Park in Loughborough. Overall, availability in FY23/24 moved up significantly to a little over 4.5m sq ft, with the greatest increase being in second hand space coming onto the market, and which now stands at a little under 3m sq ft.

Available Grade A space fell slightly to 1m sq ft, with the largest building on the market at the end of FY23/24 being the 340,000 sq ft Hinckley 340. However, there are a number of larger buildings presently under construction, particularly at Magna Park, Lutterworth, which will hit the market during 2024 and increase overall availability by almost 1.6m sq ft.

The above market summary indicates that Innes England's Leicester City commercial market has certainly started to recover from the Covid-19 downturn, and a steady growth in all sectors within the Commercial Market are evidenced. (Source: Innes England Market-Insite-2024 Brochure).

However, CoSTAR UK Market Insight for FY23/24 – Leicester City, commented that capital market valuations were down across all sectors (Industrial -0.2%; Office -3.0%; Retail -4.6%). Sale versus asking price was also down significantly, with Retail down on average -8.9% with the lowest at -14.2%; Office was down on average -0.4% with the lowest -18.8%; whereas Industrial was up 6.1% on average with the lowest at -20.8%.

There has been limited movement in The Corporate Estate portfolio in recent years, with the council holding 82.5% of its portfolio value in the traditional sectors of industrial, office and retail.

FY23/24 however, saw land values increase significantly increasing the overall value by £6m – mainly in the Office sector.

Statement by the Valuer for the Year Ending 31 March 2024

In accordance with the instructions of the Chief Finance Officer we have valued the Corporate Estate portfolio as at 31 March 2024. The valuation has been prepared in accordance with the RICS Red Book Global Standards dated 31 January 2022 published by the Royal Institution of Chartered Surveyors (RICS) and to conform with the disclosure requirements of that publication. We understand that the Valuation is used for Financial Statement purposes.

The value of the Corporate Estate portfolio asset valuations carried out in the year ending 31 March 2024 is £147,221,180 (One Hundred and Forty-Seven Million, Two Hundred and Twenty-One Thousand and One Hundred and Eighty Pounds).

The Valuation is for the sole use of the Council. It is confidential to the Council its Officers and Professional Advisors. Details of the basis of our valuation and the individual properties are set out in the valuation report dated 31 March 2024.

Gbolahan Solaymon MRICS and RICS Registered Valuer
Senior Estates Valuation Surveyor

RICS No. 1119552

Although a complex changing picture, the overall capital asset valuation* of the council's corporate estate portfolio in FY23/24 is down slightly at 2% or £3.9 million in FY23/24 — from £151 million to £147 million over the last year — mainly due to changes in lettings strategy and the sale of six post-pandemic office buildings. Generally, values were down too in the Retail sector mainly due to market risk factors relating to challenging rental values, availability and rental risk factors such as strategic redevelopment of land. Industrial values remained reasonably static year on year and Office increased significantly due to a mixture of land value increases, rent and changes in occupation and the addition of six properties, five of which had previously not been valued (as under £100k) moved into the capital asset pool for the Corporate Estate.

Chart 6 above, shows the impact of the acquisitions on sector values, with the 'other' sector now representing a smaller proportion, at around 17.5% of overall portfolio value. Whilst land and property values have remained reasonably static in the industrial sector, the sector continues to make up around one third of the value of the portfolio, topping sector capital asset value at £43 million (last year Retail was the top sector in capital asset value at £48.5 million).

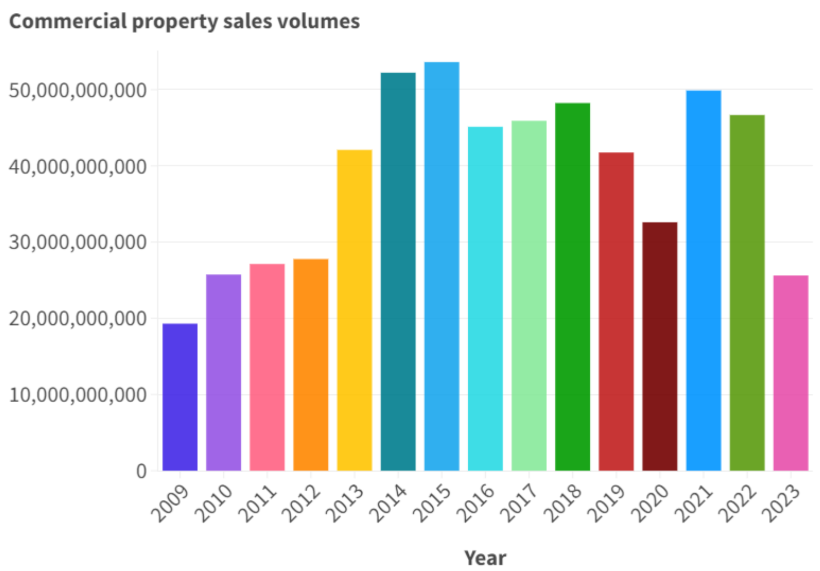
In summary, official estimates now suggest that the UK economy fell into a technical recession – defined as two consecutive quarters of falling output – during the second half of last year.

Placing substantial stress on households' finances, consumer price growth averaged 7.4% in FY23/24, with intense inflationary pressures prompting considerable tightening in monetary policy from the Bank of England.

Given the significance of this, it is somewhat surprising that consumer spending managed to avoid an outright contraction, although the meagre 0.3% rise over the past 12 months represents the softest annual increase since 2011; excluding the sudden drop during the first year of the pandemic.

Although the UK economy's overall momentum was at best sluggish last year, the mild recession that occurred could still be classified as a relatively soft landing given the steepest rise in policy interest rates set by the Bank of England over a two-year period since the late 1990s.

This – arguably – resilient picture was, nonetheless, not mirrored across commercial property markets. Data from CoStar shows total volumes came in at £26bn during 2023, the weakest annual trend since 2009 and down around 46% compared to 2022.



UK commercial property sales volumes. Source: CoStar
This dreary outcome was not unique to the UK of course, with rising interest rates in many parts of the world placing strain on commercial real-estate markets. In the US, for instance, commercial property investment levels sunk 56% year on year in FY23/24.

Despite negative economic factors, felt sharply across all UK commercial real estate markets modest recovery is predicted next year, although the impact will vary across the UK.
For now, the broad assessment for the coming year is that total commercial real-estate investment volumes should recover modestly compared to last year, although with this coming from such a low base, buyer activity will likely remain subdued when viewed in a longer-term context.

Meanwhile, headline capital values – while potentially coming under some further downward pressure over the first half of this year – should then stabilise towards the end of 2024.

Indeed, the net balance for 12-month capital value expectations, again taken from the RICS UK Commercial Property Monitor, stands at just –7% across all sectors. This reading should be interpreted as respondents envisaging a virtually flat outturn for the year to come.

Of course, not all portions of the market exhibit the same prognosis for the year ahead. With the industrial sector still displaying solid occupier fundamentals – even if tenant demand is unlikely to regain quite the same exuberance of previous years – this should provide a firm foundation for a recovery in buyer activity.

Indeed, industrial rental growth is running at an annual pace in excess of 5%, signalling that the sector continues to display strong income-producing potential for landlords.

Meanwhile, although the Office and Retail sectors nationally have also posted positive rental growth over the past 12 months – 2% for the former and 1% across the latter – the underlying picture is a bit more complicated.

For one, rising incentive levels across both – as reported continuously by RICS members in recent years – are masking trends in headline rental indices, at least to a certain degree.

Moreover, there remains a huge divide between the so-called prime portions of these sectors and the secondary ones. At the prime end, occupier demand is generally holding up well. Knight Frank research for instance shows nearly 85% of office take-up last year was accounted for by new or grade-A space.

Conversely, both secondary office and retail properties continue to see rising vacancy rates amid the ongoing challenges presented by the shift towards remote working and online shopping. As such, RICS members in aggregate anticipate further falls in rents, and capital values, across these types of property.

Therefore, even though the general market is likely to begin to recover slowly as cyclical macroeconomic pressures ease, there will remain significant structural weakness in certain sectors for the foreseeable future.

Gbolahan Solaymon, MRICS, RICS Registered Valuer
Senior Estates Valuation Surveyor,
RICS No. 1119552

* *The FY23/24 Annual Audit of Assets is in progress and will complete in October 2024. For the purpose of this report, the figures contained within for valuation will not be formally signed off until the Governance & Audit Committee in November 2024, therefore all figures and assumptions are subject to audit.*

PORTFOLIO PERFORMANCE

Occupancy:

Industrial	Office	Retail	Other	2024 Average	2023 Average	2022 Average
99%	92%	96%	95%	95.5%	96%	95%

For the 2023/24 reporting period, property availability increased slightly over the period by 0.5%. This was predominantly due to the contraction of the council's operational office estate portfolio and appropriation to the corporate estate while marketing to let took place.

The overall pace of take-up was very slow in commercial real estate globally. The demand for secondary office space in the city was not as buoyant in the first three quarters of 23/24 with the market seeing only a slight increase in demand in the last quarter of 2024. Occupation has been much slower as tenants move out of old premises, take advantage of their break clauses before they move to their new premises.

Investment in property was down in the terms of Commercial property sales volumes, with CoStar showing total volumes coming it at £26bn in FY23/24, the weakest annual trend since 2009. Property that was anticipated to be sold for office to residential conversion resulted in initial interest, however, market asset valuations were attempted to be undercut dramatically as the cost of borrowing and cost of construction remained volatile.

Increases in utility costs has also resulted in the contraction of commercial real estate tenants particularly in office and retail markets. The contraction represented lost gross rental income of £101,430 for the period — 0.9% of the annual gross revenue income based on anticipated market rents. This was also felt in both rent and lease renewals where the market is pushing for inducement.

Whilst there were a limited number of vacant spaces across each of the sectors, there has been some turnover seen across our retail sector, as business owners have chosen to move online, accept improved inducements elsewhere and relinquish space by enacting break clauses in favour of flexible working. In popular city centre industrial and office workspaces however, availability has remained limited with the majority of units being re-let.

City centre retail continues to change and evolve; however, space is at an all-time high. It is anticipated that next year, in 2024/25 with interest rates falling for the first time in August 2024, that even though the general market is likely to recover slowly as cyclical microeconomic factors ease, there will remain significant structural weakness in certain office and retail sectors for the foreseeable future. The council's strategy continues to be pragmatic in terms of strategic value, the local plan, ever-greater requirements for supported living and residential housing along with a balanced view of leisure and retail offer to support increases in inner-city living and cultural interest.

Revenue Performance:

Without significant change to the portfolio in the last year, the optimisation strategy, along with effective investment planning in previous years, ensured that the revenue position remained reasonably solid year-on-year.

This echoed the RICS UK Commercial Property monitor, in the last quarter of FY23/24, expressing that the commercial real estate market had reached the bottom of the current cycle. There have been marginal improvements have been felt across the UK and the market continues to lack significant momentum. Prime office rent expectations have gained a greater lead over the secondary market. And, occupier and investor demand remains downbeat outside the industrial sector.

The RICS UK Commercial Property Monitor for Q4 FY23/24 revealed some growing confidence in its long-term outlook. While mixed, the largest proportion of respondents in Q4 FY23/24 (33%) believe that the market has bottomed out, seemingly aiding a slightly more positive long-term outlook.

While most of the market remains sluggish and lacking momentum, there are clear incremental improvements. Occupier demand remained negative overall (-7%), although less so than previously (-12% Q3 FY23/24), and although both the office and retail sectors remain relatively weak, sentiment has improved from Q3. Industrial demand remains positive although less so from previous highs.

It should be noted that nationally, prime property continues to outperform secondary units. With footfall crucial for retail, as well as energy costs continuing to rise, the location and relative energy efficiency of prime units are likely encouraging further positive momentum.

The outlook for national prime retail rents has, for example, stabilised with the twelve-month expectations net balance moving to -4% from a value of -13% in Q3 FY23/24. In fact, this reading marks the least negative view on prime retail rents since Q1 of 2018/19.

When looking at the regional results, the national picture is largely mirrored throughout most parts of the country. For London however, the prime office and retail markets stand out as exhibiting stronger rental expectations and are firmly in the positive while secondary office space appears to be under even greater pressure across the capital. Industrial in the Midlands is particularly strong.

Overall investment demand remains relatively soft, evidenced by the all-property investment enquiries indicator reporting a net balance reading of -19%. Similarly, overseas investment enquiries also continue to slip, with all sectors seeing a decline (to a greater of lesser degree) in Q4 of FY23/24. In its Manifesto for the Built Environment, RICS called for a defined national real estate roadmap attractive to inward investment. This would be a holistic national strategy which attracts and deploys inward foreign investment on a national scale, benefitting the whole economy.

There was a notable improvement to sentiment in credit conditions reporting a much flatter -5% reading, compared to the significantly more negative -44% and -75% seen in Q2 and Q3 of FY23/24, respectively.

RICS Senior Economist, Tarrant Parsons, said: “Current conditions remain challenging across the UK commercial property market, with investor demand still being weighed down by the tighter lending climate and uncertain outlook for values. At the same time, relatively weak momentum with respect to economic activity more generally is taking its toll on tenant demand, with the ongoing structural challenges facing parts of the office and retail sectors also hampering market sentiment. That said, the significant turnaround in expectations for monetary policy in the second quarter of FY24/25, provide a reason for cautious optimism going forward, and the latest results do point to a more stable backdrop for credit conditions coming through.”

For the council’s corporate estate, FY23/24 followed the national trend with gross income down just under £200k from £11.46m to £11.27m. Gross rental income losses were due to mainly from property sales with leases. Predominantly, as result of retraction by De Montfort University’s office holdings at Leicester Castle as they sought to tighten their exposure to external leases; along with a retraction of the Council’s own office space plus the sale of 10 York Road.

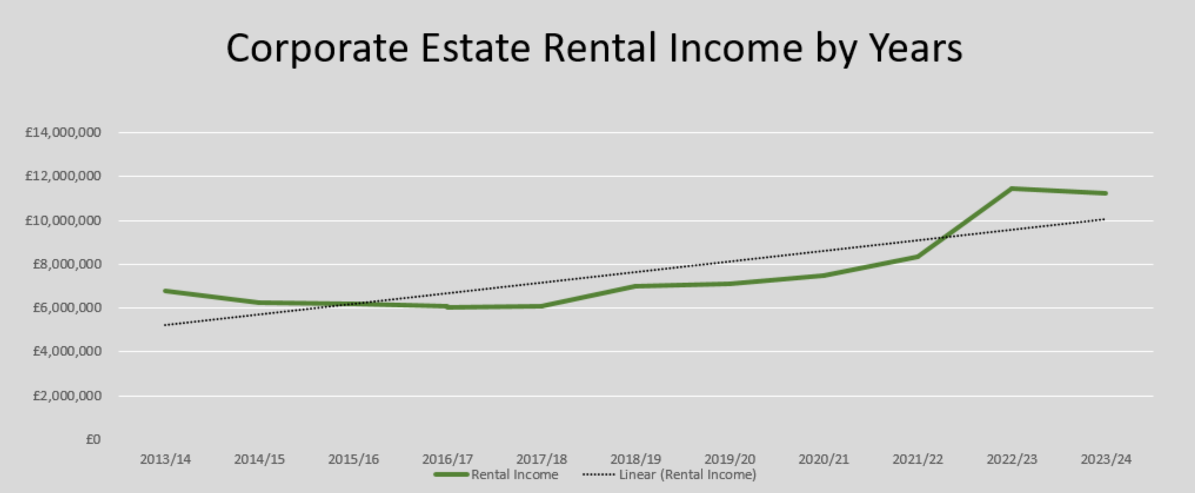
Quarterly returns as measured in the MSCI UK Quarterly Property Index, the largest UK direct real estate sample recorded returns of 0.54% for March 2024. Industrial was the best performing sector with a 3-month return of 1.12%. Retail sector recorded returns of 1.06%. Other sector recorded returns of 0.63%. The Hotel sector recorded returns of 0.16%. Residential sector recorded returns of 0.13% and Office sector recorded returns of negative 0.51%. Income return was stable in line with the previous quarters at 1.20%.

In the corporate estate the industrial sector mirrored that of the MSCI UK Quarterly Property Index, being the best performing sector, up overall by 10.78% or £311,882 on FY22/23. With marginal retail returns of £54,835 due predominantly to a solid second full year results of the Haymarket Shopping Centre. The office sector recorded lower returns predominantly due to availability, while the lowest return was in the ‘other’ sector – down 13% or -£377,199 on last year with the main drivers for this being a significant rent-fee development period and the sale of an asset.

Gross Rental Income - Corporate Estate Income by Sector:

The chart below shows the sector-by-sector gross rental income for the last decade. The corporate estate, in line with other UK property results dipped slightly overall.

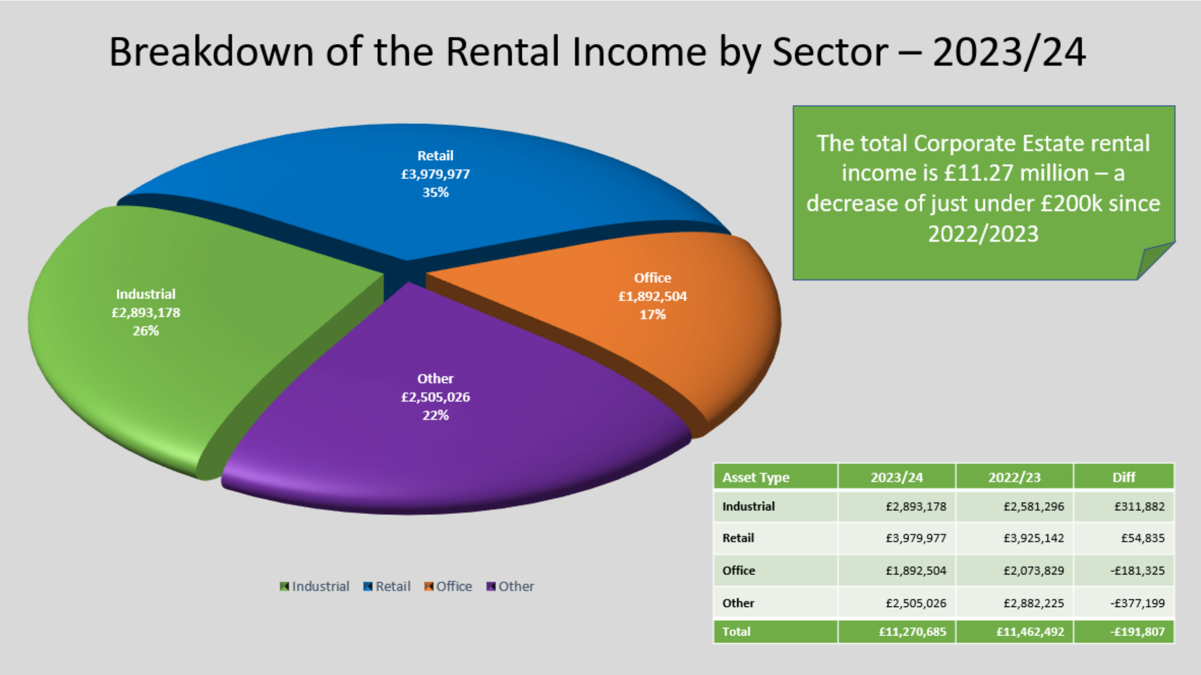
CHART 7 – CORPORATE ESTATE RENTAL INCOME BY YEARS



	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	Grand Total
Industrial	£2,537,933	£2,399,584	£2,532,444	£2,499,273	£2,513,386	£2,380,190	£2,563,544	£2,446,245	£2,581,296	£2,893,178	**£25,347,073**
Retail	£678,121	£675,269	£652,966	£658,759	£1,389,432	£1,382,731	£1,442,042	£2,332,180	£3,925,142	£3,979,977	**£17,116,619**
Office	£1,005,181	£1,221,292	£1,042,773	£1,067,692	£1,169,556	£1,300,141	£1,635,991	£1,425,684	£2,073,829	£1,892,504	**£13,834,643**
Other	£2,020,207	£1,895,656	£1,846,047	£1,882,742	£1,943,574	£2,040,916	£1,842,431	£2,133,009	£2,882,225	£2,505,026	**£20,991,833**
Grand Total	**£6,241,443**	**£6,191,802**	**£6,074,230**	**£6,108,466**	**£7,015,948**	**£7,103,977**	**£7,484,007**	**£8,337,117**	**£11,462,492**	**£11,270,685**	**£77,290,168**

The optimisation of The Corporate Estate has resulted in general improved gross income across all sectors, with industrial being least impacted by the pandemic strategically targeted first, showed a healthy increase.

Chart 8 below, shows the percentage of gross revenue income generated by each of the sectors.



Asset Type	2023/24	2022/23	Diff
Industrial	£2,893,178	£2,581,296	£311,882
Retail	£3,979,977	£3,925,142	£54,835
Office	£1,892,504	£2,073,829	-£181,325
Other	£2,505,026	£2,882,225	-£377,199
Total	£11,270,685	£11,462,492	-£191,807

The top five gross income generators represent £1.179m or 10.5% of the corporate estate.

Net revenue contribution continues to be hindered by increases in utility costs, availability, and the costs of repairing and maintaining the estate.

Maintenance and building quality/improvement plays a significant role in the short-, medium- and long-term quality of our estate and an improved commitment to maintenance and sustainability of The Corporate Estate remains a significant investment strategy. As we continue to focus on ESG and the government's implementation of the Minimum Energy Efficiency Standards in the forthcoming year, a further commitment to meeting and wherever economically viable, exceeding the Minimum Energy Efficiency Standards has been made through the introduction of the Cleaner Greener programme. EPC ratings will meet the legislative requirements and will continue in earnest along with additional capital investment in both understanding the general condition of our estate and in responding to our climate action plan and sustainability targets.

Financial Year 2023/24		
Gross Revenue Income	**Running/Management Costs**	**Net Revenue Contribution**
£11,270,686	£5,593,788	£5,676,898

Market Rents

According to the East Midlands Market Insite 2024 report issued by Innes England, the industrial market continues to deliver strong results, with good occupier demand, rising rents, generating the confidence for developer and investor support with new supply.

Derby has a strong occupier base, with Rolls Royce and the Railway related industries and is diversifying, with the largest transaction being HelloFresh (430,000 sq ft) at SmartParc's specialist food manufacturing campus. St Modwen's Phase 2 development, at St Modwen Park ensured that Grade A availability remained healthy with 145,000 sq ft of that phase already let. Prime industrial rents have grown 40% over the last 2 years and secondary rents 37%.

Prime office take-up across Derby and Leicester were above the 10-year average, so reports of the demise of the secondary office market are not reflected in our data. Investment volumes reflected the lack of activity again in FY23/24 and it's no surprise that two of Innes England's largest deals were the sale of a multi-let industrial estate of 165,700 sq ft and the acquisition of a new build PRS scheme, comprising 34 units, both market sectors in strong demand.

Despite continued economic pressures, the UK and East Midlands retail sector has experienced a brighter outlook over the course of FY23/24 than in previous years, however, it is still the most challenging sector.

National retail vacancy rates across high streets, shopping centres and retail parks have reached their lowest point since the first half of 2021 at an average of 13.27%, with the East Midlands sitting at 15%. Whilst shop closures have reached their highest level since 2020, the amount of retail openings achieved their highest level since 2014, reflecting our reputation as a 'nation of shopkeepers'. National and regional chains continued to rationalise their high street portfolios with local independents taking advantage of the rebased rents.

The new Rateable Value assessments came into effect in April 2023 reducing many rates bills for both national, regional, and independent occupiers. Following the Autumn Statement, many retailers were delighted to hear that the Small Business Rates multiplier will be frozen at 49.9p until April 2025 and the Retail, Hospitality and Leisure scheme will be extended for the fifth year running, providing eligible properties and businesses with up to 75% rates relief up to £110,000 of Business Rates per business.

Whilst national headline rents have not yet returned to pre-pandemic levels (and, it might be some time before they do), net effective rents have almost returned to figures being achieved before the pandemic. It is important to note both headline and net effective rents have seen increases from FY22/23, having improved year on year by 3.3% and 2.5% respectively.

FY23/24 saw another retail giant fall with the failure of Wilko's significantly affecting many parades, retail pitches and local shopping centres where they were anchoring tenants. To the relief of some landlords, Poundland and B&M have agreed to take on 71 and 51 stores respectively, with 56 stores already reopened and trading as Poundland. This leaves over 200 store futures uncertain, with landlords working creatively with occupiers to find a solution.

Roadside retail continues to flourish, with existing operators remaining acquisitive and more roadside operators entering the market. However, rising costs of construction have led to an increase in rents being demanded by developers, which coupled with delays in the planning process has created a lag in delivery.

Leicester

Retail performance within Leicester was mixed, with Highcross entering receivership in March 2023 and the centre seeing a number of notable closures including Ted Baker and L'Occitane. Despite the troubled financial situation, there were positives with Holland & Barrett, Ann Summers moving from Haymarket and Breitling opening throughout the year, with Luke 1977 relocating to the former Sharps store.

Other notable openings within Leicester City Centre include the reopening of the former Wilko's on Charles Street as Poundland, Roxy Ball Room opening in the former DW Sports on Humberstone Gate and Shoezone opening along Gallowtree Gate, in the former Barnardo's premises. Varanasi, a regional Indian restaurant, has opened a 6,000 sq ft restaurant along High Street in the former Red Hot World Buffet. Finally, Pragnell has opened new premises along Market Street.

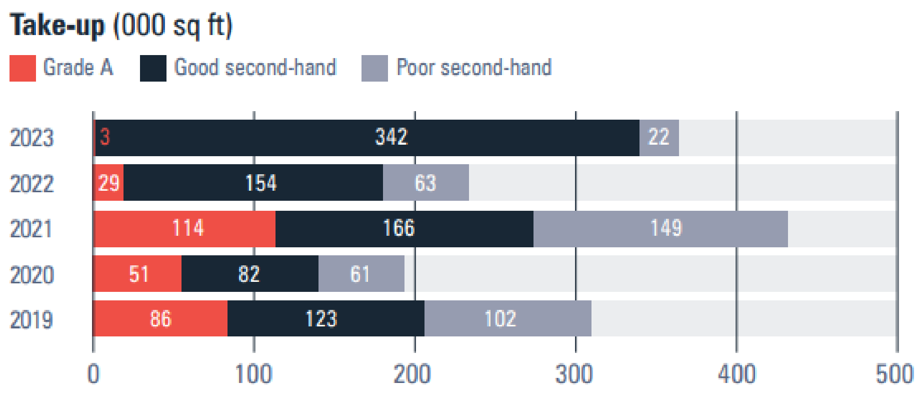
In contrast, Fosse Park continues to go from strength to strength with Dreams, Natuzzi, and Designer Sofas opening within the former Argos store, which has been reconfigured to provide 3 in line units. New Look has relocated into the former Outfit premises, with works currently being undertaken at their former unit. Footasylum has refurbished their existing unit between JD Sports and River Island, which included an expansion from 4,000 sq ft to 6,400 sq ft.

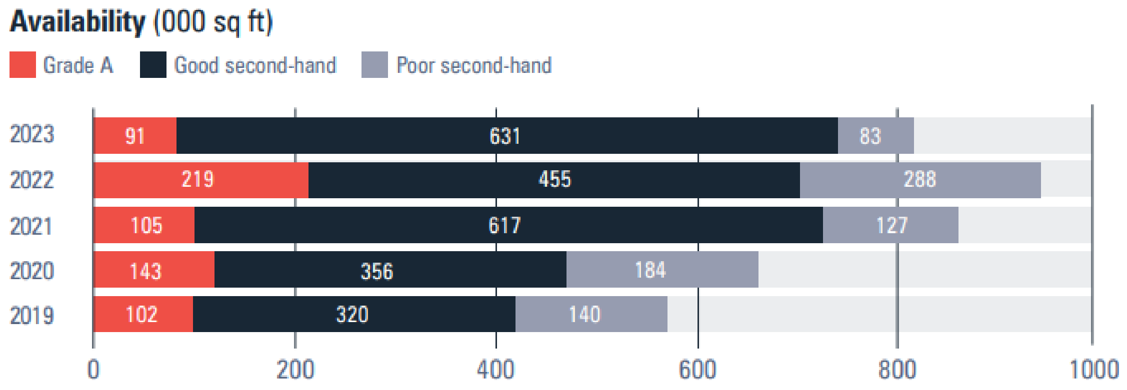
The development drive within Leicester has continued, with the Waterside Regeneration entering its 10th year, which has included 1,000 new homes and the construction of over 90,000 sq ft of office space accommodation. This council-led project has attracted more than £300 million of new investment to Leicester. This investment has included the construction of 900 apartments, accommodation for c. 1,000 students, a new school with a capacity for 1,200 pupils and two new hotels.

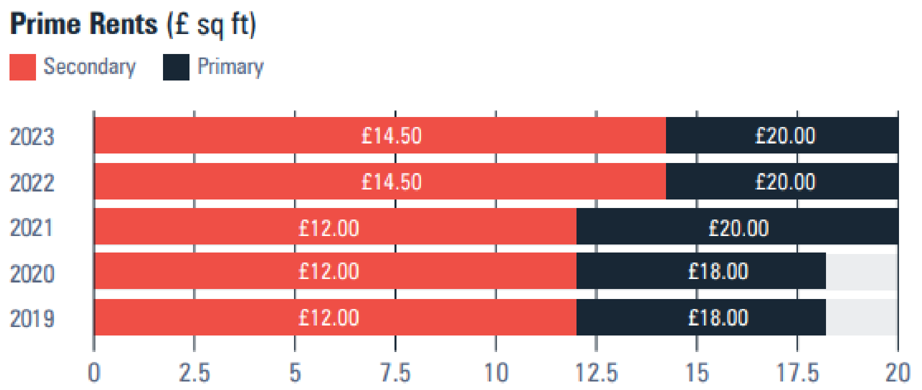
Leicester Market redevelopment started at the end of last year, with the aim to modernise the 700-year-old marketplace. The council has also proposed the demolition of buildings to the north of Green Dragon Square, with the aim to improve the connection of the Market and to Cank Street and St Martin's Square.

Office take-up in Leicester moved back above the 10-year average in late 23/24, with total activity of 366,740 sq ft. Sales and lettings were primarily focused on second hand space, with two-thirds of activity out of town.

The largest letting was at Granite House on Watermead Business Park, Thurmaston, where E.ON took 24,863 sq ft. The largest transaction in the city centre to an occupier was the freehold purchase of Bankfield House on New Walk, by Planet Education Networks of 14,554 sq ft. Supply tightened, falling to 805,322 sq ft, with the main focus being on second hand space, which now accounts for 93% of stock on the market. Grade A supply overall stands at 90,840 sq ft and is primarily focused out of town at Carlton Park, Narborough. Supply within the city centre is as low as 16,200 sq ft. Rents remained stable at 2022 levels, with prime values at £20.00 per sq ft and secondary rents at £14.50 per sq ft.

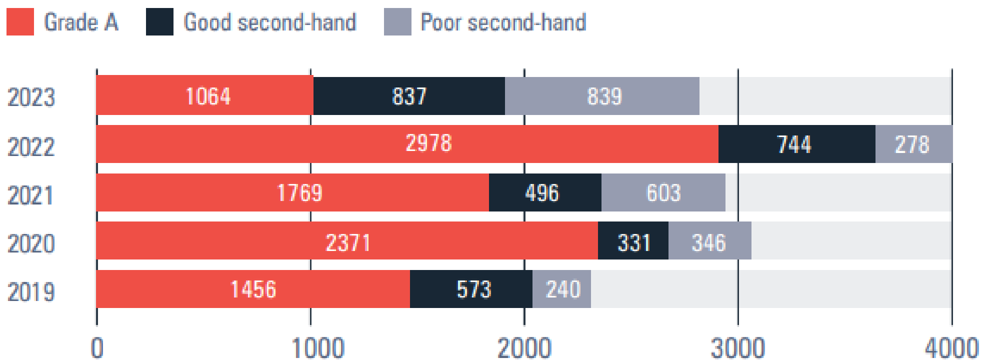




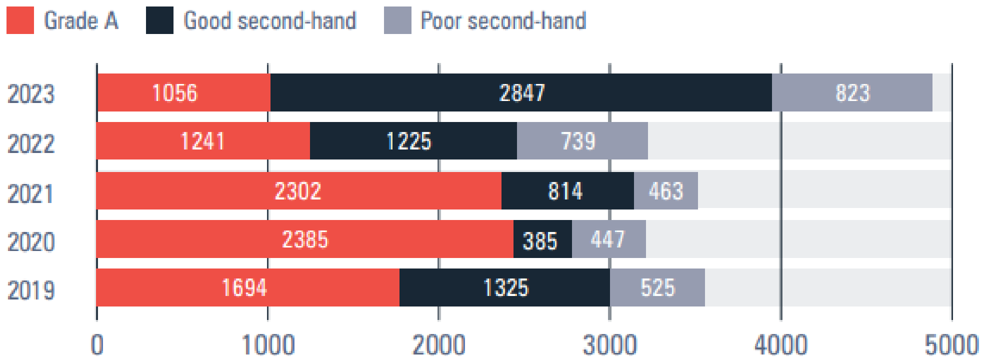


Industrial take-up remained above the 10-year average for the fourth successive year in FY23/24, with total activity of 2.7m sq ft. The 'Big Box' market continued to see good levels of activity, with six deals totalling 1.25m sq ft. The largest deal was the 493,000 sq ft build to suit deal for Persimmon's timber frame manufacturing subsidiary Spring 4, at Garendon Park in Loughborough. Overall, availability moved up significantly to a little over 4.5m sq ft, with the greatest increase being in second hand space coming onto the market, and which now stands at a little under 3m sq ft. Available Grade A space fell slightly to 1m sq ft, with the largest building on the market at the end of the year being the 340,000 sq ft Hinckley 340. However, there are a number of larger buildings presently under construction, particularly at Magna Park, Lutterworth, which will hit the market during 2024 and increase overall availability by almost 1.6m sq ft. The availability of poorer quality Grade C accommodation remained similar to 2022 at 823,000 sq ft. Prime rents edged higher to £9.00 per sq ft, growth of 5.9% over the 12 months, whilst secondary rents continue to reflect the strength of the market, rising to £7.00 per sq ft.

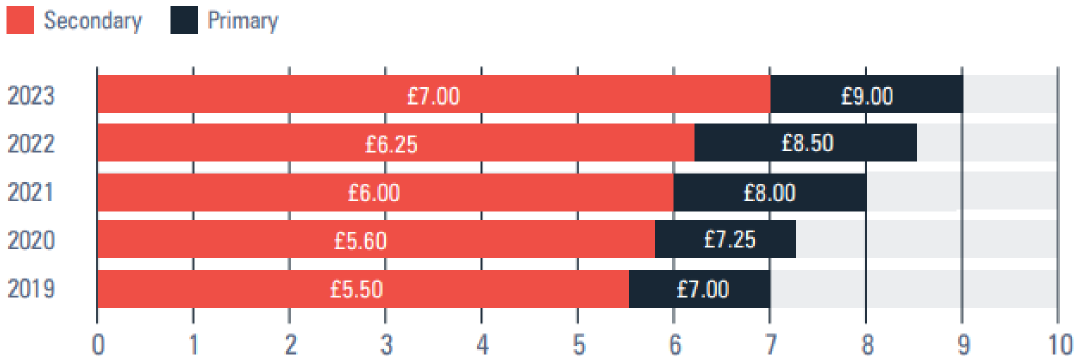
Take-up (000 sq ft)



Availability (000 sq ft)

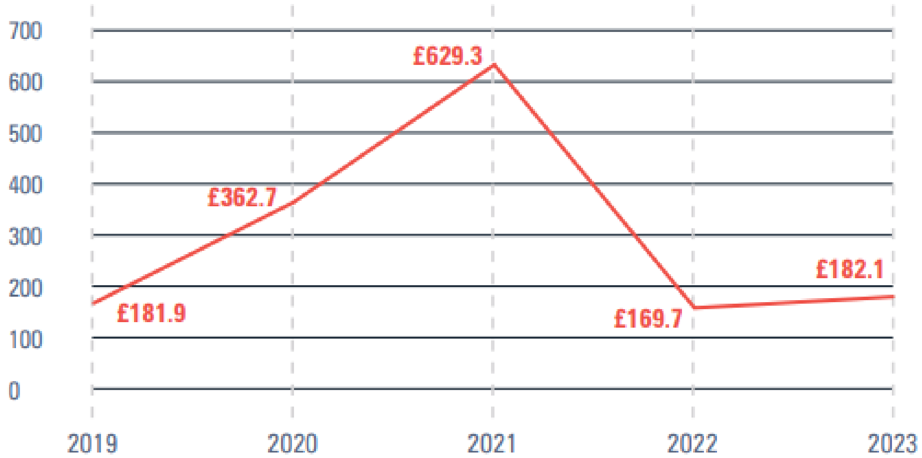


Prime Rents (£ sq ft)

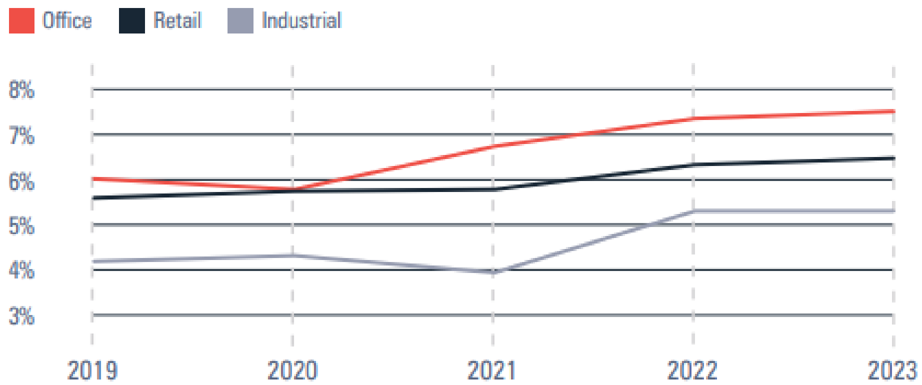


Investment activity in Leicestershire edged up to £182m in FY23/24, with the main focus of activity continuing towards the industrial sector, which accounted for 47% of the year's transactions. The largest deal was the £29.75m purchase of the 297,300 sq ft Tesco Chilled distribution facility at Hinckley by global logistics real estate group Realterm US. The purchase price represents a net initial yield of 7.6% and reflects the impending lease expiry. The most significant deal outside of the industrial sector was the £25m purchase of Meridian Leisure Park, Leicester by Greenridge Investment Management. The park provides 155,100 sq ft of space, with tenants including Vue Cinemas, Hollywood Bowl, David Lloyd Health Clubs along with a number of restaurants. The purchase price reflected a net initial yield of 8.5%. Overall prime yields continued to drift out over the year by 25 to 50 basis points.

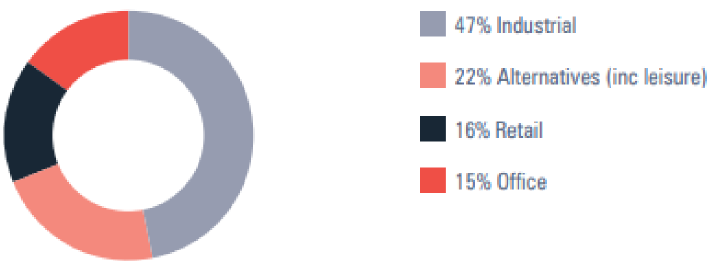
Investment across the County (£m)



Prime Yields



Investment by Sector



Key Highlights:

Offices:

Prime headline rents: £20 per sq ft
Secondary rents £14.50 per sq ft

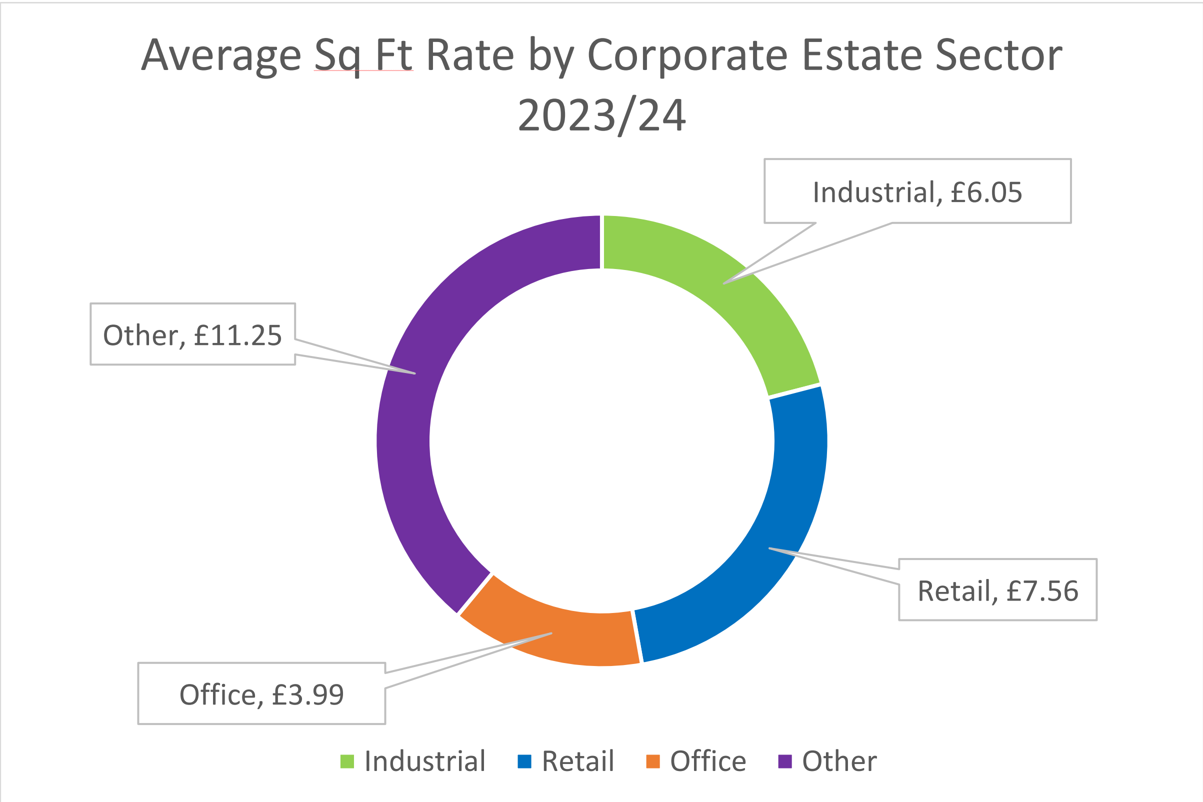
Industrial:

Prime headline rents: £9 per sq ft
Secondary rents £7 per sq ft

Investment:

Transactions Completed £182.1m

The council's corporate estate continues its optimisation progress in earnest with improved resources across the team, completing a root and branch review of all rents. Industrial edged up from £5.40 per sq ft to over £6 per sq ft with further gains anticipated with the purchase of the Heathers Industrial Estate in FY23/24 and a review of secondary office and industrial at our business centre workspaces. Retail dropped slightly to £7.56 per sq ft from £8.42 per sq ft due to availability and inducement. Secondary office rents lag the market significantly with optimisation of this sector to come in the next 12-18 months as the secondary office market starts to pick up.



Yield:

According to Savills (Market in Minutes: UK Commercial March 2024) the national market remains in a period of stasis, with a slow start to the year and limited evidence to move yields, but opportunities are emerging. ‘Rest of UK offices’ look interesting based upon the yield gap to Central London offices.

The UK average prime gross yield of 6.14% showed no change.

At present, there are fewer sellers at current pricing; however, going forward, with falling interest rates, lower debt rates will bring in more geared capital. The UK investment volume data for the first quarter, albeit subject to upward revision, is showing c.£8bn. At this trend rate, for the remainder of this year, it would show a 12% increase on the £28.4bn total recorded for FY23/24.

A driver of increased investment volumes could be regional offices. Despite historically sitting in line with retail and industrial yields, long term, the current office prime yield is higher than both sectors for all the reasons that have impacted on the office sector since the pandemic. Additionally, the current yield gap between London and the rest of the UK is 2.6 percentage points, the highest for over 32 years.

As UK office occupancy rates continue to climb, albeit slowly, the question is whether the office sector outside of Central London is showing the most interesting opportunity. A driver would also be an acceleration of a return to the office. The higher productivity discussion of homeworking versus office work, which has been ongoing since the pandemic, is turning towards performance, i.e. not just what is being done, but how well. Employees may say their best performance is at home; the C-suite is not so sure.

Yields continued to present a very mixed story across the board. Outward pressure can be seen in four sectors of High Street Retail (7%), Prime market shopping centres (8.25%), Offices (7%) and Industrial (5.25%).

The Corporate Estate returned an average gross yield of 7.66% for the year ended March 2024, which is considered ‘very good’ in commercial real estate market terms, and significantly above the average UK prime rates of the CCLA property funds.

This compares with the CCLA Local Authority Property Fund (used as a benchmark) which returned a gross yield of 4.84% in FY23/24.

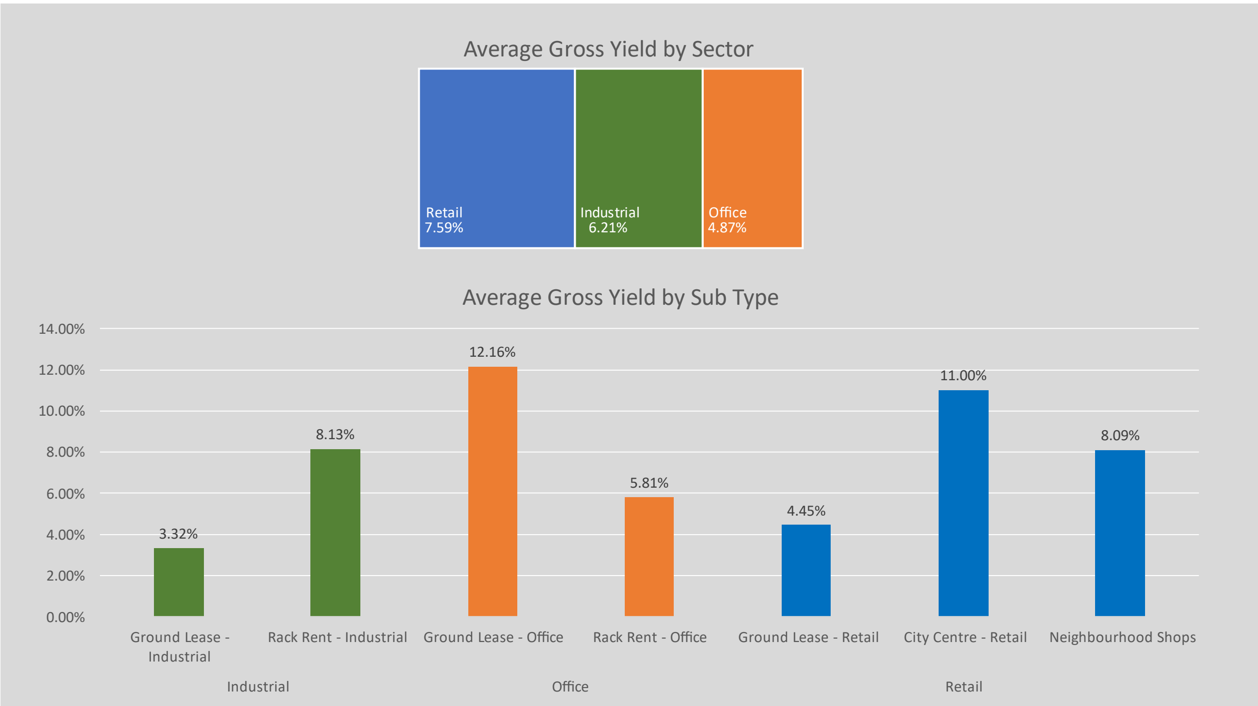
The Chart below, illustrates the average gross yield by sector for the three main sectors in the last financial year, with the Retail sector returning the highest average yield at 7.59%, and the Industrial sector close behind at 6.21% — both above the performance achieved in FY22/23.

Net yield is down predominately due to the upwards pressure in increased utility costs driven largely from increases in electricity and gas due to the Russo/Ukraine War. This is expected to continue into FY2024/25, with some small reduction in the summer months which increased again in the final two quarters from 1 October 2024. Continued increases in the cost of construction and the scarcity of certain supplies, continue to impact repair and maintenance costs.

The strategic decision to reduce the council's operational office estate has also had an impact on the corporate estate as some sites are waiting to be leased or on hold due to a difficult seller and borrower market.

It is important to understand that, in calculating yields, the capital valuation of a portfolio is a significant factor. In line with what has been happening in the rest of the UK, local land values have generally appreciated although, as previously stated, in the case of The Corporate Estate portfolio, such appreciation generally relates to development value rather than existing use of the land. Instances where land and property valuations have decreased minimally, such as the neighbourhood shops, means that yield is affected positively. When we look at the yield performance of some of the sub-sectors, we can see a clearer picture in terms of performance, with a number of sub-sectors generating excellent gross yields above 8% with ground leases in the office sector taking the top spot versus the rack rent office yields and rents being at an all-time low and down considerably on last year at 5.81% mainly due to availability as noted above. City centre retail gross yields remain excellent at 11% but down 5.59% on last year due predominantly to a competitive retail space market and inducement.

CHART 9 – AVERAGE GROSS YIELD

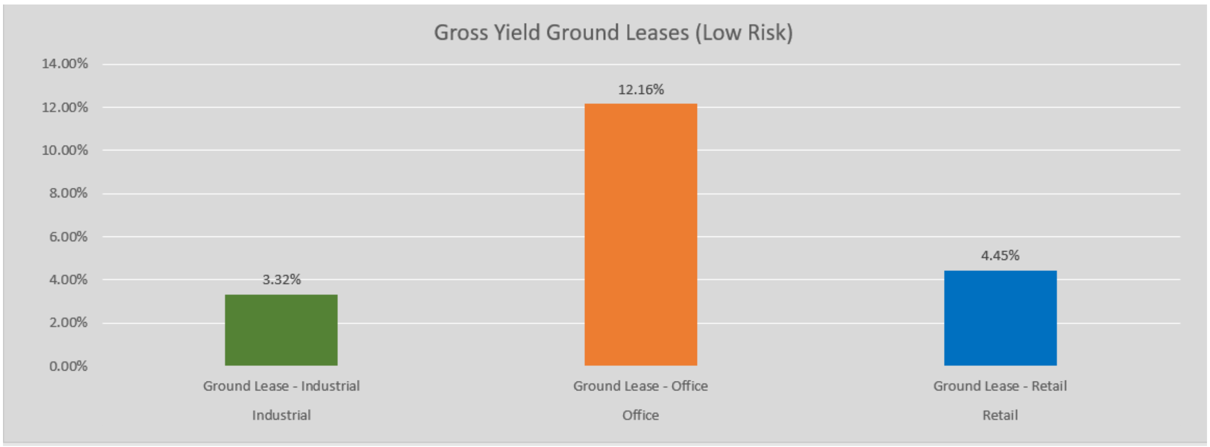


Yield in Detail:

Gross yield is generally used to compare the financial performance of property investments and as noted above, they are influenced by the quality of the assets (e.g. location, sector, condition, supply and demand) and the associated investment risk. With a balanced portfolio, the corporate estate therefore incorporates some 'gold thread income returns' for very low risk investments over longer term investment periods.

Ground leases are generally held in the portfolio as steady, long-term leases that have a strategic role in minimising the revenue risk of the corporate estate as a whole. Whilst ground leases in the three main sectors are generally lower than average performers, the impact of planned rent increases in recent years — particularly in the office sector — means that yield performance has increased significantly with Ground lease office sector increasing from 8.32% to 12.16%.

CHART 10 – GROSS YIELD GROUND LEASES



Ground lease industrial = 3.32%
Ground lease office = 12.16%
Ground lease retail = 4.45%

It should be noted that a lower yield is not necessarily due to poor performance (and is not always of concern), as low yields are generally related to the low risk involved with the investment. Examples in the corporate estate include our ground leases — that provide a long-term income — as well as the neighbourhood shops that we hold for purposes that are secondary to income generation.

The average net yield of 3.86% achieved in FY23/24 by The Corporate Estate is on a par in performance in comparison to CCLA Local Authorities Property Fund (2023/24) at 1.11% net yield used as a benchmark) with the council achieving yields — subject to sector — ranging from 3.32% to 12.16% respectively.

CHART 11 — YIELD CONTRIBUTION BY SECTOR SUB-TYPE

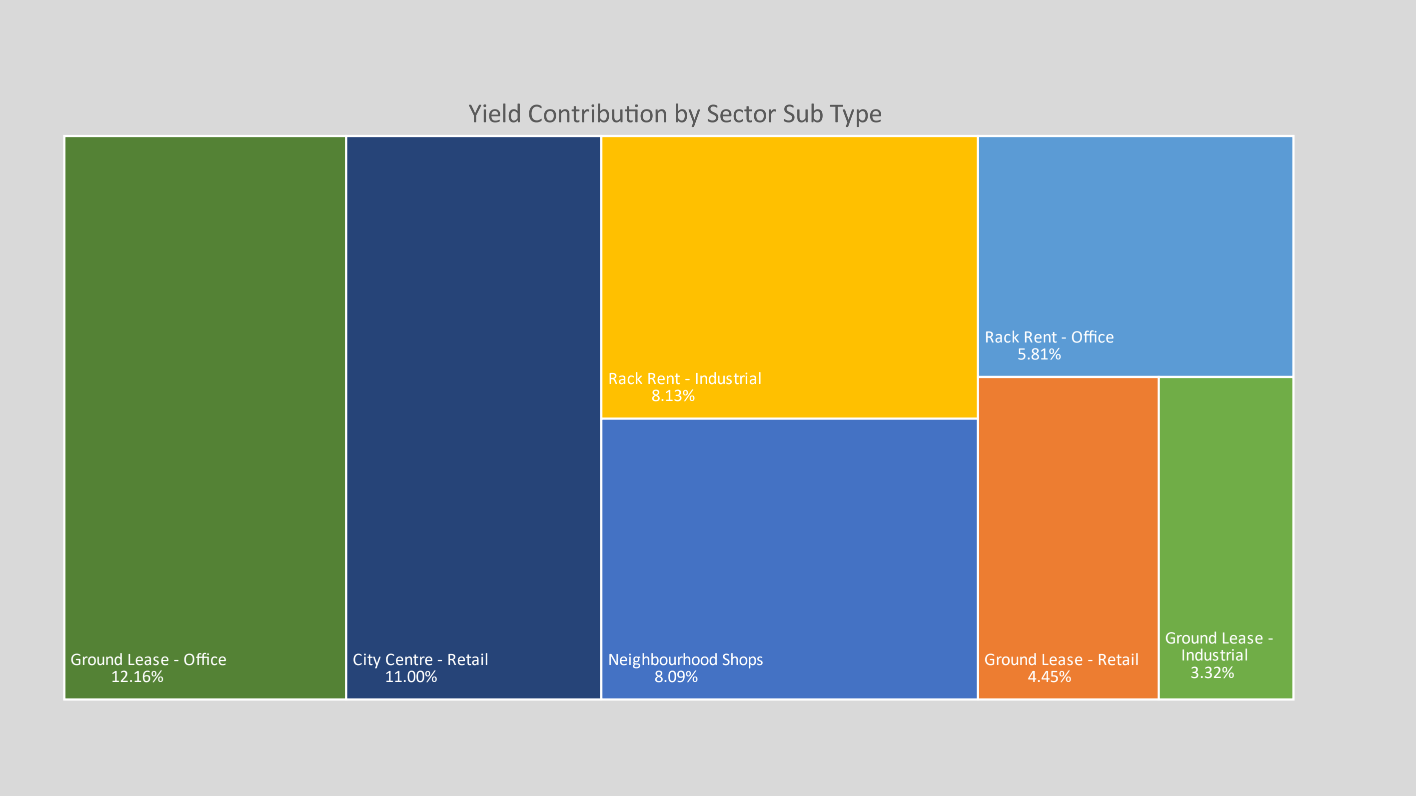


Chart 11 (above) provides a breakdown of yields across a range of sub-sectors within the Retail, Industrial and Office sectors. The Rack Rented Industrial sector has consistently performed very well for some years, and continues to do so, with an upwards shift of 0.2% for the year ended March 2024 to 8.13% (demonstrating and excellent average gross market yield).

Despite the continued general economic turbulence in FY23/24, the best performing sector in terms of yield for the third year in a row was the city centre retail sector at a staggering 11%. Both city centre retail and the neighbourhood shops have achieved an excellent yield of over 8.09% this year, and the Haymarket Shopping Centre shows its good solid performance from its full-year results. Office ground leases increased significantly to 12.16% from 8.32% due to a combination of capital asset valuations and long lease reviews in-year.

Portfolio Sector	Yield	Indicator	Performance Review
Industrial:			
- Ground Lease Industrial	3.32%	Lowest Yield/ Low Risk/ Stable	Slight increase from 2022/23. Our industrial ground leases are generally long-length leases that are low risk in terms in terms of demand and rent volatility and offer us stability and longer-term sustainability – hence the lower-than-average yield.
- Rack Rent Industrial	8.13%	Very Good Yield	A well- performing sector with long-term tenants that continue to have confidence in the Council as their landlord. up from 2022/23 levels, with opportunity to increase further as rents continue to be aligned to market rates.
Office:			
- Rack Rent Office	5.81%	Good Yield/ Some Risk	Down from 2022/23 levels due to increased availability. There continues to be some risk in this sector in the future as working practices and hybrid working changes.
- Ground Lease Office	12.16%	Excellent High Yield / Low Risk	Increased from last year, these low-risk ground leases provide a stable and sustainable revenue income.
Retail:			
- City Centre Retail	11.00%	Excellent High Yield/ Turbulent	City Centre retail space that brings in an excellent yield. Yield performance is high due to the historic nature of the holdings and subsequent high values, although an increased capital valuation in 2023 – due to rising land values and growth in sector holdings - has resulted in a reduction in yield despite 2023/24 seeing increased revenue returns from rent. A full year of solid income and improved capital asset value from the Haymarket Shopping Centre continues to prove a good investment.
- Ground Lease Retail	4.45%	Good Yield/ Low Risk/ Stable	A slight decrease, however, a good solid yield. Longer-length leases with a lower risk that the City Centre retail space. A stable performer with low risk attached.
- Neighbourhood Retail	8.09%	Very Good Yield/Held for Community Benefit	A slight decrease in yield compared to 2022/23 as availability has increased due predominantly to capital requirements. Based in community settings on our local authority housing estates, and generally tied to our housing portfolio by way of flats above the shops, this sector is held to provide communities with local, convenient, neighbourhood shopping facilities, which are now undergoing improvements to shop fronts to bring locality improvements.

The Haymarket Shopping Centre

In the third year of ownership, our short-term goals of continuing to stabilise the performance of the asset, build a single, strong management team and improving the asset's performance in terms of availability remain our key focus. We have also been proactive in securing long-term sustainable income streams with quality occupiers, most notably agreeing a 15-year extension to the lease with Tesco and with Addict Dance Academy moving to the Haymarket Theatre to bring a vibrant start to FY23/24. Improved occupancy rates have the potential to improve income further as secondary retail offers good value for money in the market.

6. CLIMATE EMERGENCY

The council has developed our next Climate Ready Leicester plan which has a key focus on the decarbonisation of our buildings, which contribute over 60% of our carbon emissions. This work will be delivered through three key strands: energy demand reduction, efficiency improvements and heat decarbonisation.

Our Clean and Green programme has just launched as a new initiative that will pave the way for identifying actions that will deliver cost and energy savings. Starting with energy saving initiatives such as LED lighting and Solar PV, and also exploring new technologies and partnerships to enhance our buildings and ultimately reduce our energy consumption. We are also continuously seeking out further funding for decarbonisation work through regional and national funding programmes.

There are three key actions in our Climate Ready Leicester plan that are currently being delivered through the Corporate Estate:

- **Compliance with the MEES legislation - Commercial Buildings (Minimum Energy Efficiency Standards)**
    - Ensure that council commercial properties meet the Minimum Energy Efficiency Standards:
        - Currently an Energy Performance Certificate (EPC) rating of 'E' or above
        - Expected to rise to C or above by April 2027 and B or above by April 2030.
- **Energy saving in void buildings and spaces**
    - Review and improve the way we manage energy to minimise wastage in void buildings, end of lifecycle buildings and parts of buildings awaiting redevelopment.
- **Ian Marlow Centre redevelopment**
    - Redevelopment of the former Ian Marlow Centre for employment use focusing on fabric performance and sustainable energy generation throughout the specification.

This year has seen work begun on the Ian Marlow centre redevelopment with the creation of new business units which will have PV panels and a range of energy efficient characteristics as well as EV charging points. Tenants of these buildings will be signing up to our future new green lease scheme. The Corporate Estate will continue to seek funding opportunities to develop and enhance the energy efficiency of the buildings in our drive towards net zero.

Anna Dodd - Energy and Sustainability Manager

Joanne Allen - Head of Sustainability

Statement of Assistant City Mayor Environment and Transport

The role of the Corporate Estate in delivering the council's net zero aspirations has two opportunities.

Firstly, there is the opportunity and obligation to provide potential tenants with energy efficient buildings, as required under the MEES legislation which came into force in 2023/24.
Secondly, by delivering suitable wellbeing, sustainability, and new technologies through improved workplaces we can demonstrate leadership in educating and supporting our tenants to act on their impact on their environment, contributing to theirs and our own environmental, social and corporate governance (ESG) responsibilities.

I am pleased to see us tackling the carbon emissions from our buildings, as there is no route to net zero without substantial change in the built environment.

I am particularly excited to see the redevelopment of the Ian Marlow Centre and the creation of our first new green leases at our industrial business units as a demonstration of a leading sustainable approach of practical delivery and influencing behavioural change.

Councillor Geoff Whittle

Assistant City Mayor for Environment and Transport

7. FINANCIAL STATEMENT

Corporate Estate Out-turn for the Year Ending 31 March 2024:

Number of units – 1263

Valuation as at 31/03/24 - £147.2m

The Corporate Estate net return to the Council for the financial year ending 31st March 2024 was £5.68 million. Income generated from these assets is included in the Council's revenue budget.

It was previously highlighted that guidance from MHCLG (Ministry of Housing, Communities & Local Government) and CIPFA (Chartered Institute of Public Finance and Accountancy) warns against investment activity which is disproportionately large in relation to an authority's finances.

With land and property investment income from The Corporate Estate accounting for 1.57% of the Council's net revenue budget in 2023/2024, it continues to represent a manageable risk in relation to the overall revenue budget.

Stuart McAvoy
Head of Finance

In accordance with the Council's Capital Strategy approved in February 2024 and to be updated in February 2025, the Council will not make commercial investments primarily to generate income. Each investment will benefit the Council's service objectives.

Acquisition of commercial or industrial property can be considered where there are either economic development or service reasons why the city would benefit from the Council's ownership. An example of economic development reasons might be to facilitate a significant business relocation to the city or surrounding area.

Construction or development of commercial or industrial property can be considered for regeneration purposes within Leicester, Leicestershire, and Rutland area where the asset constructed or developed would generate a continuing income stream and have a readily realisable capital value.

Low Carbon Energy Investments which help to reduce climate change can be considered. Any such investment will still be expected to make a positive return, though in making the investment the Council will consider the environmental and social benefits as well as the financial return.

Whilst investment in existing corporate estate properties can be considered, government rules no longer allow investment in new corporate estate properties primarily to produce income even when this is funded from the sale of existing properties; there has to be a main service objective for the acquisition of new properties.

Nick Booth
Treasury Manager

8. MANAGING RISK

In managing its portfolio of commercial land and property, Leicester City Council has the following risk management arrangements in place:

- An Investment Strategy considered by council, that limits the exposure of the council's in terms of property investment.

- A varied and balanced land and property portfolio that spreads risk across a number of sectors and investment types.

- A strategy that prioritises security over yield and provides a commitment to support the local economy by providing accommodation for local businesses.

- Contributing 1.57% of the council's 2023/24 net revenue budget, income from the council's portfolio of land and property represents a manageable risk in relation to the overall budget.

- Robust governance and transparency around proposed commercial acquisitions and disposals and the performance of The Corporate Estate, ensuring that appropriate due diligence is undertaken in making estate management and investment recommendations.

- A diverse directly employed team with a range of commercial and estate management expertise ensuring the authority has the skills and capacity to make investment recommendations with due regard to risk, and to manage the investments over the long-term.

- In order to maintain capital asset valuation, capital investment will continually be required in order to shoulder the increase in maintenance costs to maintain the quality of the estate and meet ESG and MEES targets over the short- to medium term.

The council's corporate estate portfolio has remained stable in recent years in terms of its asset numbers, its make-up in terms of sector classification, its overall capital value, and its income.

With recent uncertainty in the market, our strategy to optimise the performance of our existing estate and to take our time in considering our investment and growth options has proved to be a sensible one, with a further strategic acquisition of the Heathers Industrial Estate in Q4 2023/24 likely to have a further positive impact on a very solid portfolio performance despite a difficult year economically.

9. FUTURE OUTLOOK AND STRATEGY FOR 2024/2025

This outlook utilises the most recent and relevant data available at the time of publication of this report (October 2024).

The RICS UK Commercial Property Monitor Q4 2023/24 states that the polarisation in market between prime and secondary property is expected to continue to grow. Leicester City Council's Corporate Estate is predominantly secondary in nature, with economic regeneration projects making up for the majority of new 'prime' accommodation investment. The RICS continues to emphasise that:

- Headline tenant demand and investment enquiries metrics remain flat.
- The London office market continues to see stronger activity relative to the rest of the UK.
- The overall UK commercial market is still widely seen as either at the bottom of the economic cycle or in the early stages of an upturn.

In the East Midlands, there still appears to be a general lack of confidence within the market. Investment continues to be challenging due to the economy in general. Those who are investing are looking for exceptional capital asset asking price reductions against market value – challenging disposal values. The Bank of England base rate was cut for the first time since 2020, bringing relief to many households and businesses struggling with higher costs and loan repayments. Interest rate reductions in August 2024 is seen economically as a positive to entice borrowing and calm the markets. However, the rate cut from 5.25% to 5% split the Monetary Policy Committee (MPC) voting 4-for and 4-against. Andrew Bailey made the casting deciding vote which passed the reduction. Generally, the capital values market is at best 'luke-warm' with under market value transactions indicating that those seeking land and property for their own investment purposes are striking hard deals. Many sellers are not transacting, and sales asset volumes are down. There is definitely an air of caution over acquisitions and disposals which will hopefully dissipate over the coming months.

Long over-due reforms in UK planning systems are welcomed by the market against a challenging and inadequate construction workforce in terms of delivering economic growth. So, overall, a relatively flat headline picture for the market.

In keeping with the steady tone to the latest data, the headline occupier demand series posted a net balance of +4%, identical to the reading seen last quarter. Given this value remains very close to zero, it suggests tenant demand trends were more or less stable. At the sector level, the office and industrial categories posted net balances of +7% and +10%, pointing to a marginal pick-up in occupier demand in both cases. Conversely, the net balance of -5% registered for the retail sector, although slightly less negative than the -10% reading seen previously, continues to point to subdued momentum behind tenant demand.

Alongside this, space available for occupancy rose modestly across the office and retail sectors, albeit the pace of increase softened slightly compared to last time (in net balance terms). Interestingly, vacant space reportedly edged up slightly within the industrial segment, evidenced by a net balance reading of +9% being registered in Q2 FY24/25. This marks a departure from the almost uninterrupted decline in the availability of industrial space over the past decade.

Looking ahead over the coming twelve months, rental growth projections continue to point to a mixed performance across different asset classes. Still leading the way, prime industrial rents are seen rising over the next year by a net balance of +59% of contributors. At the same time, secondary industrial rents are also expected to move higher, albeit the net balance of +22% is noticeably more moderate than that for prime. Meanwhile, the prime/secondary split remains even more pronounced for offices, with the twelve-month rental expectations series posting a net balance of +45% across the former and a still firmly negative -32% for the latter. Looking at the prime retail sector, a net balance of +10% of respondents now foresees rents increasing over the year ahead. Although the latest figure is relatively modest, it does represent the most positive reading for this metric since 2017. Nevertheless, secondary retail rents continue to exhibit a negative outlook, posting a net balance of -32%.

At the regional level, the outperformance of the prime office market in London continues to come through in the latest expectations data. Indeed, a net balance of +68% of respondents covering London foresee prime office rents rising over the year ahead. This stands significantly above net balance readings of +29%, +25% and +29% for the South, Midlands and the North respectively.

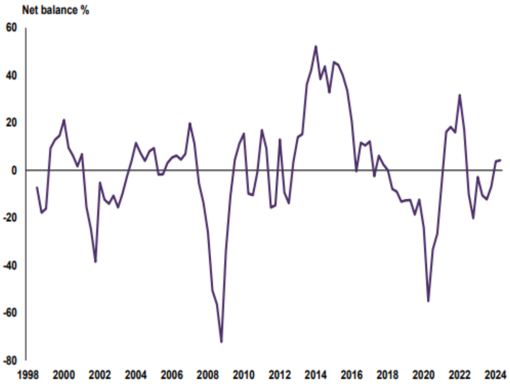
Looking at the investment market, the all-sector net balance for investment enquiries came in at -4% in Q2 FY24/25, completely unchanged from Q1 FY24/25. As such, this measure is signalling a stagnant trend in investor demand of late. At the sector level, industrial properties did attract another small rise in buyer interest (net balance +10%), while slightly negative net balance readings were returned across the office (-9%) and retail (-18%) sectors.

Over the next twelve months, a net balance of +57% of survey participants foresees capital values rising across the prime industrial sector, with the figure standing at +19% for secondary. In both cases, these forward-looking readings are marginally stronger than last quarter. Across the prime office sector, a net balance of +38% of respondents expects capital values to move higher, up from a reading of +25% in Q1 FY24/25. By way of contrast, a net balance reading of -33% in Q2 FY24/25 shows that secondary office values are still seen coming under downward pressure over the next twelve months, even if this is slightly less negative than the reading of -41% seen in Q1 FY24/25. For prime retail properties, a net balance of +12% of contributors anticipates an upward trend in capital values, up from a reading of +5% beforehand. Again, secondary retail is still seen struggling, with capital values expected to fall according to a net balance of -29% of respondents.

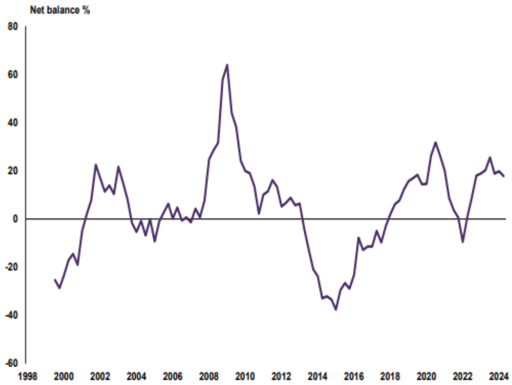
Away from the traditional sectors, both capital value and rental growth projections remain firmly positive for several alternative commercial real estate asset classes. In particular, student housing, data centres, life sciences and multi-family residential all exhibit solid expectations for the year ahead. At the other end of the spectrum, the outlook is much flatter for the leisure sector, although this does mark an improvement compared to the marginally negative assessment respondents put forward last quarter (Q2 FY24/25).

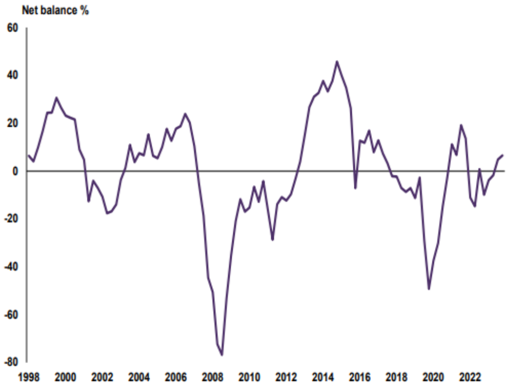
Commercial property all-sector average

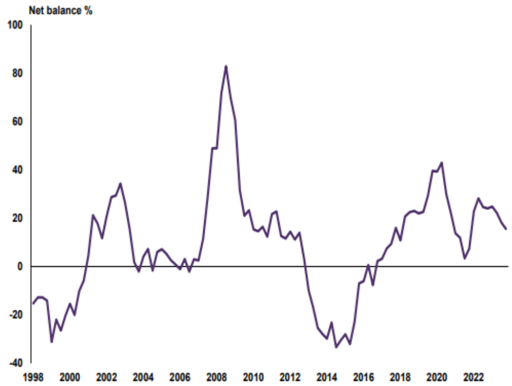
Occupier demand



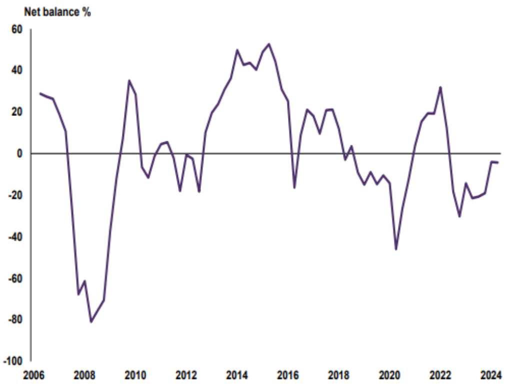
Availability



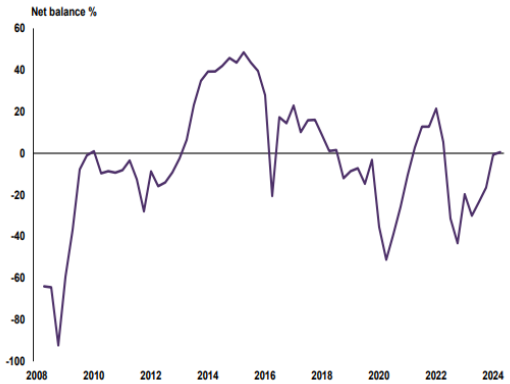




Investment enquiries

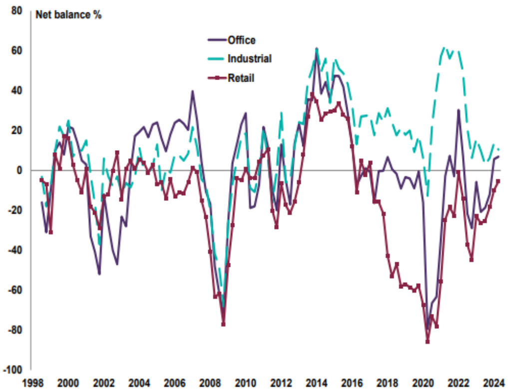


Capital value expectations

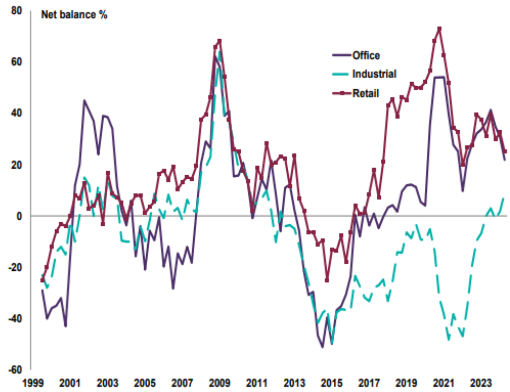


Commercial property - sector breakdown

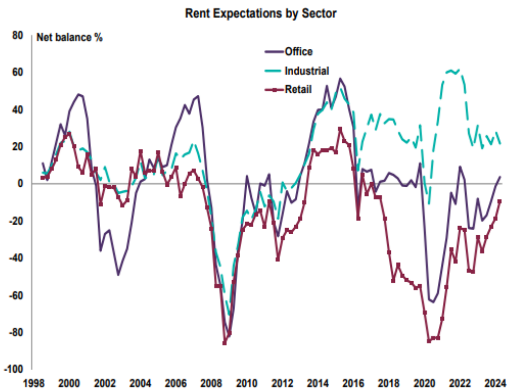
Occupier demand



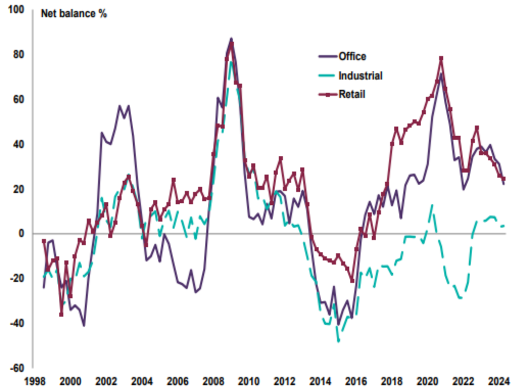
Availability



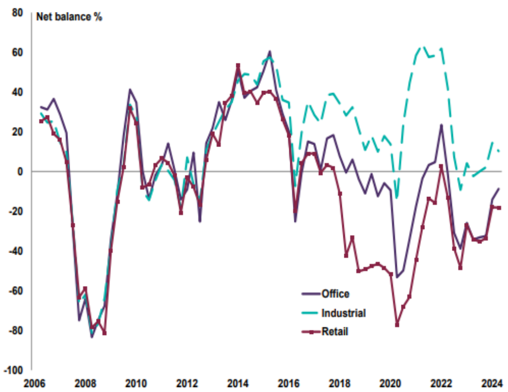
Rent expectations



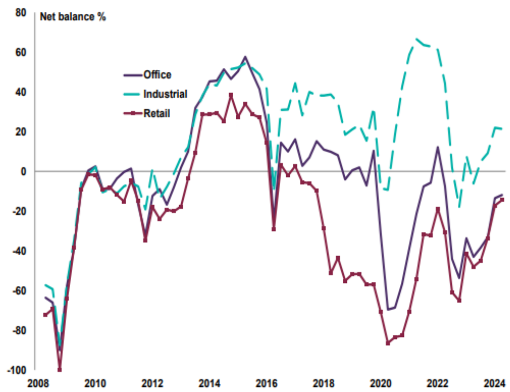
Inducements



Investment enquiries



Capital value expectations

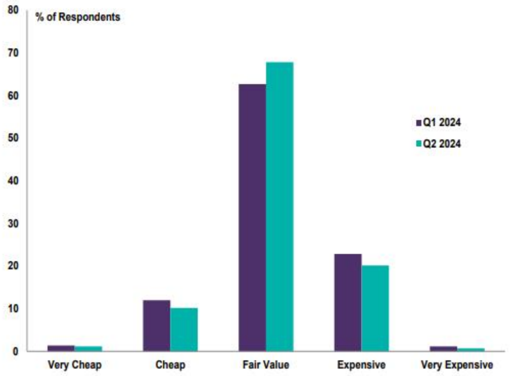


Commercial property - additional charts

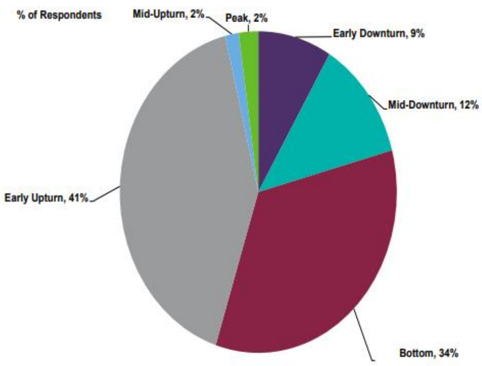
12-month capital value expectations

12-month rent expectations

Market valuations



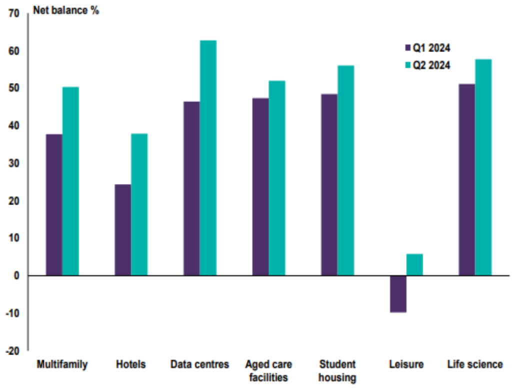
Property cycle



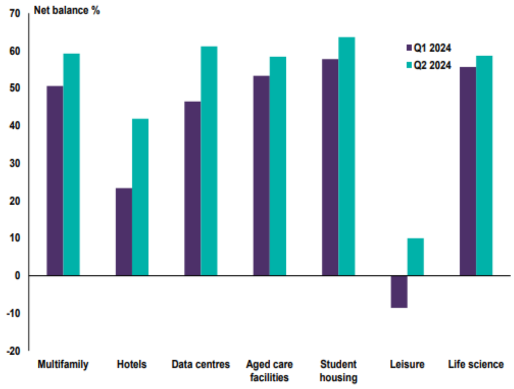
12-month capital value expecations alternatives

12-month Rental expecations alternatives

12-month capital value expecations alternatives



12-month Rental expecations alternatives



Other important metrics include:

- Annual CPI inflation increased slightly to 2.2% in July 2024, up from the recent lows of 2.0% recorded in May and June, as last year's declines in energy prices fall out of the annual comparison. Therefore, we have now probably passed the bottom of the current cycle. Whilst a further uptick in inflation is likely this year, this should only be modest. The consensus forecast is for CPI to reach 2.5% by Q4 of FY24/25, whilst the Bank of England now expects around 2.75% in the second half of this year.

- Economic growth has bounced back strongly from the very mild technical recession in the second half of FY23/24. Q1 FY24/25 saw growth of +0.7%, its highest rate since Q2 2021 (at the tail end of the post-pandemic recovery period), followed by +0.6% in Q2 FY24/25.

- Growth is likely to slow somewhat in the second half of 2024/25. However, with the path of interest rates now downwards (albeit gradually), much improved consumer confidence, and strong levels of business confidence being reported in recent PMI surveys, the outlook is for further robust rises in output. The latest (August) consensus expects +0.4% in Q3 and +0.3% in Q4 of FY24/25. Overall, FY24/25 is forecast to see annual GDP growth of 1.1%, rising a little to 1.3% in the first quarter of 2025.

- The Labour government's large overall majority should provide a welcome period of relative domestic political stability. Encouragingly, its manifesto acknowledged the importance of economic growth and contains several positive initiatives, including developing an industrial strategy, and policies to accelerate the upgrading of key infrastructure and to raise the rate of housebuilding. However, delivery will be extremely challenging, and the government is clearly signalling that a further rise in taxation will be announced in the forthcoming Budget on 30th October 2024. This will need to be carefully targeted if it is to avoid adversely impacting confidence and growth.

Retail occupier market:

- Retail sales have been highly volatile this year, impacted by factors such as the unpredictable weather and the general election. Sales volumes rose 0.5% during July, a significant improvement on the (upwardly revised) -0.9% during June. Department store sales surged by 4.0% month-on-month, and other non-food stores rose by 2.5%. The overall trend in sales volumes is one of gradual improvement. Taking the three months to July 2024, volumes rose by 1.1%, the second-strongest rate in almost three years.

- GfK's Consumer Confidence series was unchanged in August 2024 at -13, but nonetheless remains at its highest level in almost three years. The index for personal finances improved, likely helped by August 2024's base rate reduction, although consumers remain downbeat about the broader economy.

- Households are benefiting from this year's reductions in National Insurance Contributions, and many lower income households are also benefiting from April 2024's uplift in the National Living Wage of nearly 10% (though this is adversely impacting costs for many businesses, most notably the retail and food & beverage sectors). In addition, wage growth continues to be well above inflation, and the energy price cap continues to fall. This is all positive for household disposable income. However, tax increases are likely to be announced in the October's 2024 Budget, although it remains to be seen where the burden will fall.

- The Q2 2024 RICS UK Commercial Property Survey shows a net balance of -5% for retail occupier demand, a noticeable improvement on -10% in Q1 2024, -18% in Q4 2023, and -25% in Q3 2023. Respondents continued to cite an increase in overall vacant space.

- Average retail rental values have shown very modest growth since 2022, according to MSCI. The Monthly Index reports that average retail rental value growth in the 12 months to July 2024 was 0.9%, and has been within a range of 0.5% to 0.9% on this measure since October 2023. However, average retail rental values remain 16.5% below their previous peak in 2018.

- The all-retail trend masks significant variation, depending on the type of property and location. Average rents for standard (high street) shops fell almost continuously from May 2018 to May 2023, by circa -29%. However, growth has returned over the last year. Annual growth accelerated to 1.9% by May 2024, although it slowed to 1.0% over the year to August 2024 (MSCI Monthly Index). Growth is being driven by the London market.

- Average rental values in the retail warehouse subsector are continuing to rise, by 1.4% in the 12 months to July 2024, unchanged from June 2024 and slightly above the previous peak in annual growth seen in January 2023 (MSCI Monthly Index). On a quarterly basis, growth increased a little to 0.5% in the three months to July 2024, a little above the equivalent annual rate.

- Average shopping centre rental values have also returned to growth in recent months, rising by +1.0% in the three months to July 2024. This has not yet fed through to the annual figures, although July's decrease of -0.5% was a significant improvement on the fall of -1.3% recorded in June 2024, and the slowest rate of decline since May 2023.

Office occupier market:

- The longer-term impacts of the working-from-home revolution mean that many businesses have been assessing their real estate footprint, although the level of downsizing is highly business-specific and has now declined noticeably. Indeed, occupancy rates have broadly levelled off, and the three-day office week has emerged as the new normal.

- Although corporate real estate is the second-highest cost after salaries for many businesses, the provision of high-quality space remains important to assist with recruitment, retention, and productivity strategies, as well as to enhance staff health & wellbeing. This is reflected in continued robust demand for high-quality space.

- There is also a much greater focus on buildings that are sustainable and energy-efficient, as occupiers try to meet increasingly ambitious ESG aspirations. This is being accelerated by the changes to MEES regulations which came into force in April 2023, with the next round of tightening due in 2027.

- We are seeing continued strong demand for serviced and co-working provision from established businesses that wish to lease short-term space, pending a move to longer-term conventional office space once the economic outlook becomes more certain.

- The Q2 2024 RICS UK Commercial Property Survey continues to show a positive net balance for office occupier demand at +7%, up slightly from +6% in Q1 2024, and a considerable upturn on the negative balances reported throughout FY23/24. This upturn in sentiment has been largely due to a marked improvement in central London, and in prime office markets more generally.

- Prime rental levels have proved highly resilient, reflecting the focus of occupier demand towards top-quality space of which there is little available stock. Recent development schemes have set new benchmarks in several central London districts and regional city centre markets. The gap with rents for poorer quality grade B stock is likely to widen further.

- Average annual rental value growth for all UK offices was 2.2% as at July 2024, compared with a recent peak of 2.8% in March 2024, but well ahead of the post-pandemic low of 0.8% recorded in January 2023 (MSCI Monthly Index).

- There is an increasing geographical divergence in rental performance. Central London is pulling ahead of the south-east and regional markets, boosted by strong performance in the West End, with healthy demand for grade A stock amid a very low supply of prime space.

- Average annual rental growth in the West End/Midtown submarket reached 6.7% in July 2024 on the MSCI Monthly index, up from 6.1% in June 2024, and the highest rate since August 2016. In contrast, the City of London saw annual growth of 1.6% in the year to July 2024, down from a recent peak of 2.3% in May 2024. The rest of the south-east recorded average annual rental growth of 0.9% in July 2024, continuing a deceleration from 2.0% in January 2024. Average rental growth in the regional markets was 1.3% in July 2024, down from 1.4% in June 2024 and a peak of 2.4% in January 2024 (MSCI Monthly Index).

Industrial occupier market:

- Industrial and logistics take-up has reduced following the exceptionally strong demand experienced during 2020-2022, driven by pandemic-specific requirements as well as accelerated change in global supply chains. Longer-term structural change continues to generate occupier demand, most notably the influence of e-commerce, with ‘last mile’ units for urban delivery being a key area.

- Occupier demand for larger distribution units has been somewhat subdued in recent quarters, amid political uncertainty and elevated interest rates. However, occupiers may now be looking ahead to lower interest rates, more sustained economic growth and an increase in consumer optimism. The Q2 2024/25 RICS UK Commercial Property Survey showed a net balance for industrial occupier demand of +10%, compared with a recent low of +3% in Q3 2023, although still well below the peak of +49% in Q2 2022.

- Vacancy rates have been rising over recent quarters, due to a combination of slowing demand and rising supply. However, the supply of high quality, energy efficient new units is very limited across many key markets, which is where demand is focused, particularly as many logistics operators are promoting their ability to maximise their clients’ sustainability credentials within the supply chain. Whilst new schemes are coming forward, the overall development pipeline remains restricted, and so the relative shortage of large high-quality units will continue.

- Competition amongst occupiers for existing and new build product has helped maintain upward pressure on rental values despite the overall lower demand levels. Average annual industrial rental value growth peaked in August 2022 at 13.2% and has since decelerated from this very high rate but remains strong at 6.3% in July 2024 (unchanged from the May and June 2024 figures), still well above general inflation. Average industrial rental values increased by 1.3% during the three months to July 2024, the equivalent of 5.4% on an annual basis (MSCI Monthly Index).

- The Q2 2024 RICS UK Commercial Property Survey reported a net balance of +59% expecting prime rents to rise over the next 12 months, almost unchanged from the Q1 2024 reading. A net balance of +22% expected secondary rents to increase (unchanged from Q1 202).

The performance of our portfolio, despite the economic and market turbulence, shows that the outlook for our corporate estate remains solid, although the anticipated growth in hybrid working undoubtedly affected the demand for office space and we will need to maintain high quality space that meets the MEES legislative changes to ensure that occupancy levels and yields remain high. In addition, we should consider the opportunities to continue to develop our space to attract and meet the growing demand for flexible, local, shared office space solutions — presenting an opportunity to enhance and strengthen our local Managed Workspace offer.

According to Steven Lang, Director of Office and Life Sciences at Savills UK (Market in Minutes: UK Commercial — March 2024) “The market remains in a period of stasis, but opportunities are emerging, ‘Rest of UK offices’ look interesting based upon the yield gap to Central London offices”.

The strength of our existing Industrial portfolio, along with our ability to maintain almost 100% occupancy, tells us that our investment activity should continue to be focussed on this sector. Supply of available industrial space is shrinking, particularly in car servicing and whilst demand is high, and optimising and investing in our stock will support a growth in rental and capital values in the coming years, in a sector that currently presents low risk. Whilst supporting our city centre and neighbourhood shopkeepers in a changing market is key in terms of offering more flexible lease structures, we can continue to maintain strong asset values and improve the vibrancy of our city centre and neighbourhood shopping spaces by investing and increasing the service life — and the energy efficiency — of our stock. This includes both our indoor and outdoor space use, potentially transforming and/or repositioning some of our assets to mixed use in order to optimise benefits and to maintain an attractive retail proposition in the future.

With the Haymarket Shopping Centre under our belt, we continue to assess the potential for more beneficial use of the land in our existing portfolio, whilst maintaining the necessary balance across a broad range of sectors to minimise risk.

Short Term Strategic Focus — Consolidation, Optimisation and Targeted Investment

In our last report we set out our Strategy and the areas of activity that we are focusing on in our management of the council's corporate estate portfolio. With a short-term focus on Consolidation, Optimisation and Targeted Investment, and a medium to long-term focus on Sustainable Growth, we are pleased to report significant progress in relation to the following key strategic activities:

1. **Income and Yield Enhancement by Making the Most of our Current Portfolio:**

   • **Ensure that all tenants are paying appropriate market rents**
   We are reviewing our leases, modernising lease covenants as appropriate, and ensuring that our rents are competitive and in line with market rents. We expect to generate revenue growth of more than 10% from this activity. We are developing a transparent decision-making framework in relation to requests for below market value (BMV) commercial rentals. In addition, we are introducing improved policy provisions for rent review periods, conversion to geared leases, break clauses and lease length to support future revenue growth and risk management.

   • **Provide more transparent service charge information to tenants and improve the service charge collection process**
   We have improved the quality of our service charge schedules and are ensuring that Annual Service Charge Schedules are to RICS Standards with enhanced direct debit collection processes.

   • **Re-purpose appropriate surplus operational assets to continue to offer secondary office/ business space**
   Phoenix House and Sovereign House — have improved occupancy in the second quarter of FY24/25 – showing that there is a slight upturn in demand for secondary office space in the corporate estate portfolio. This is constantly being balanced against the need to raise capital to support our revenue position wherever possible.

   • **Maintain high occupancy and minimal void periods through improved property marketing including introducing an on-line, interactive property shop**
   We are developing our specification that will enhance digitalisation of our workflows and channel shift our enquiry management processes to improve the customer experience.

2. **Risk Management:**

   • **Review our Retail Strategy to challenge our objectives and determine the level of our future presence**
   We have adopted a Retail Strategy that recognises our commitment to maintain a city centre retail presence, supporting the retail recovery through flexible leases and incentives, along with additional planned investment and strategic acquisitions such as the Haymarket Shopping Centre; and that continues to acknowledge the importance of our locally based shops in serving the communities. We are continuing to invest in condition surveys and improvements in the Neighbourhood Retail sector and through shop front and locality improvements.

• **Capitalise on opportunities to decarbonise our estate in line with MEES legislation**

The commercial real estate sector can play can an important role in realising UK net zero ambitions if government strategy and sector collaboration is targeted at decarbonising building stock, mitigating them against changing climate and meeting sustainable investment demand.

Having delivered the £24 million funding programme to decarbonise our operational buildings we continue to seek and apply for every funding opportunity to decarbonise our corporate estate and improve our energy efficiency. Development of our new low carbon business units at the former Ian Marlow Centre demonstrates our commitment to driving forward to reach our net zero ambitions.

3. **Customer/Occupier/Tenant:**

• **Continue to support the local economy by maintaining a balance of commercialism and social value in our property offer**

In addition to adopting our Retail Strategy, we are developing a strategy for our Managed Workspaces and reviewing our holdings in the 'Other' sector (such as car parks, garages and residential).

• **Manage our tenant debt sensitively (both short-term and aged debt)**

We continue to work with our occupiers on ensuring that we liaise closely with tenants to provide and support affordable financial solutions, as appropriate, as well as signposting to grant/funding opportunities. We have made significant in-roads reducing our debt levels. On-going close management and an improved focus on personalised support and relationships with our tenants will be our continued focus on customer service improvement.

• **Transition of regeneration workspaces to The Corporate Estate (based on an agreed regeneration to commercial lifecycle)**

Leicester Business Centre transferred from our Economic Regeneration portfolio to our corporate estate portfolio. With the addition of managed workspace assets such as Dock 2, 3 and 4 and the Gresham Building to the Regeneration portfolio along with Pilot House in 2025. As part of our review of our Managed Workspace offer we have invested in new green leases and BREEAM excellent new industrial units at Blackbird Road, which will come online in 2025/26. This demonstrates how we can target investment in modern small business units for start-ups and medium-sized grow-on space to support local business growth and in continuing to meet changes in business working practices.

We are continuing to focus on Sustainable Growth and our medium to long term objectives to:

• Invest in our high-performing and strategically important sites to provide a secure and sustainable revenue income.

• Consider disposal of ageing/difficult to let/sub-optimal/end of useful lifecycle estate.

- Consider investment opportunities with strategic value in lower-risk growth sectors such as industrial, food or retail distribution/warehousing — sale and leaseback opportunities reduce risk further.

- Work with OPE partners to enhance inward investment opportunities.

- Invest in evidence-driven local growth (identifying sites for potential construction of new units/being responsive to the Local Plan).

- Consider new sector investment opportunities.

Market Commentary:

This year's forecasts suggest a stronger outlook and opportunity for UK property investment in 2024/25 compared to last year, but the political landscape and interest rate story will remain prevalent drivers.

2024/25 will be an opportunity to buy at the very bottom of the cycle.

We believe that the factors that drove the recent collapse in commercial property values and confidence will all improve in 2024/25. However, as the storm surge of high inflation and interest rates recedes, some new (and old) rocks will be exposed to challenge investors in certain sectors.

While we do expect that borrowing costs will fall over the next two years, they will not return to the levels that we were used to in the pre-Covid decade. This will mean that not only will prime yields not return to 2019 levels, but also that stronger than normal levels of rental growth will be needed to support some investment and development decisions.

Parts of the UK commercial property market look set to continue to deliver strong rental growth, but even this positivity may not be enough to convince some investors to return to the market when other regions of the world are continuing to experience falling values and distress.

Political change seldom impacts the commercial property market.

The UK is one of 40 countries that had a general election in 2024, and the question always comes round as to whether this heightens investor uncertainty. Our analysis suggest that transactional activity is generally lower than normal in the three months prior to the election date, and is then expected to recover in the following six- to twelve- month period. There is little evidence that a UK general election has ever had a measurable impact on commercial property pricing.

Given the importance of North American investors in the UK market, the fact that they too have an election this year is also a consideration around investor confidence. We find little evidence that a change of leadership in the US has ever notably affected American real estate investors' international behaviour.

Will 2024/25 be the year that offices stop being a dirty word?

There is no doubt that some offices and office markets are facing challenges, but we believe that 2024/25 will be the year when investors stop making sector-wide pronouncements and start to focus on the traditional asset-specific basics. A year ago we were predicting that prime office rents would grow across the UK, and sure enough, they did (averaging 4.2% per annum growth over the post-Covid period).

Cooling inflation, falling borrowing costs, and good rental growth prospects will bring some development schemes back into viability territory in 2024/25. This will lead to a rise in development and refurbishment starts.

Problems will remain, either where tenant demand has moved on or where the landlord has underinvested to stave off technical obsolescence. 2024/25 will also see some lenders taking a more forceful stance with borrowers, and this will lead to motivated sales at discounted prices.

At the other end of the spectrum, the undersupply of prime and green office space across the UK's major office markets remains a fact, and will continue to be a driver of better-than-average rental growth over the short to medium term. Value-add investor demand will deepen in 2024 to capitalise on this, though larger projects will remain challenged by institutional caution.

As is often the case, the first signs of recovery in capital values will come in the markets where income-focused equity investors tend to play, and we expect to see prime yields hardening in both London City and West End offices by the end of 2024.

Retail looks cheap.

Some of the pressures on household finances will diminish in 2024/25, but high prices will remain the norm in many areas, and higher borrowing costs will impact on housing expenses even after the base rate has started to fall. Many retailers will be feeling the benefit of rebased rents and rates, but also the pain of higher operational costs in other areas. Some cautious expansion of retail footprints is expected in 2024/25, and this will continue the downward trend in vacancy rates that we started to see in FY23/24.

Opportunistic investors will continue to be attracted to parts of the retail market by the high yields on offer, as well as the medium-term capital growth upside that could come from change of use. We do not expect to see a surge in retail investment volumes in 2024/25, but some prime yield hardening in some sectors and locations is baked into our forecasts for both 2024 and 2025.

From sheds and meds to logistics and life sciences.

Every recent investor survey, including our own pan-European survey from October 2023, has suggested that not only are logistics and life sciences at the top of investors' shopping lists for 2024/25, but the weighting towards these sectors has risen. Both sectors offer an attractive mix of structural change-driven demand, restrained supply, and strong rental growth prospects, so it is easy to see why income-focused investors continue to be enthused by them.

Sheer weight of money targeted at these sectors should not only lead to their prices rising in 2024, but also raises the risk of an over-exuberant period of growth thereafter. However, with annual rental growth prospects in the high single digits per annum, the rationale for buying while these sectors are comparatively cheap remains a good one.

Savills (UK Cross Sector Outlook – Commercial 2024/25)

Investment Overview - Leicestershire

Investment activity in Leicestershire edged up to £182m in 2023/24, with the main focus of activity continuing towards the industrial sector, which accounted for 47% of the year's transactions. The largest deal was the £29.75m purchase of the 297,300 sq ft Tesco Chilled distribution facility at Hinckley by global logistics real estate group Realterm US. The purchase price represents a net initial yield of 7.6% and reflects the impending lease expiry. The most significant deal outside of the industrial sector was the £25m purchase of Meridian Leisure Park, Leicester by Greenridge Investment Management. The park provides 155,100 sq ft of space, with tenants including Vue Cinemas, Hollywood Bowl, David Lloyd Health Clubs along with a number of restaurants. The purchase price reflected a net initial yield of 8.5%. Overall prime yields continued to drift out over the year by 25 – 50 basis points.

Innes England (Market Insite Brochure 2024)

It was a challenging 2023 for global commercial real estate (CRE), with investment volumes falling by 46% as investors grappled with elevated interest rates and higher debt costs. Despite a tougher environment, private investors remained the most active global buyers for the third consecutive year, taking a record 49% share of this global $698 billion market with the living sectors, industrial and logistics, and offices their top picks.

High-quality and well-managed commercial real estate is integral to levelling up UK towns and cities and contributing to better spaces and amenities for local communities. Every pound spent in the sector has the potential to generate an almost equal amount to UK GVA, so this should be maximised through a strengthened global inward investment strategy.

The UK commercial real estate sector underpins local jobs and business that can make a significant contribution the UK growth. The sector's contribution is equivalent to 3.3% of total UK gross value added (GVA) and generates 2.5% in tax revenues and the employment of 3.5% of the UK workforce through direct, indirect and induced activity.

The Wealth Report 2024 – Knight Frank

10. CLOSING STATEMENT

The resilience of our investments across the Corporate Estate continues to remain strong despite the ongoing economic uncertainty across investment markets this year. At under 2% of the council's overall net revenue budget, our Corporate Estate doesn't expose us to significant risk around macro market fluctuations, but we remain vigilant and are working hard to continuously improve our returns as well as the value of the service that we provide to our tenants across the estate.

The Corporate Estate continues to provide good economic investment, performing above CCLA trends, bringing with it a solid year of results in the performance of our portfolio in a challenging market. Whilst the economy has been volatile, its impact and pressure on our financial performance has been well-contained, with demand and occupation remaining high, and voids remaining low.

Being mindful of the prevailing fiscal pressures, we will continue to resource around protecting the value of our estate as well as improving our customer experience and aligning the council's revenue from rent and service charges in line with the market. And, whilst economic growth is not predicted in the next financial year, other social, political, and environmental factors could mean that we must adapt. We therefore plan over the next three years to change our strategic decision-making around targeted investment and disinvestment of our wider estate, allowing for the private sector to support regenerative schemes and economic development of the city and neighbourhoods.

We continue to actively focus on our net zero ambitions and sustainability remains at the forefront of our strategic improvements including a cleaner and greener property portfolio. FY23/24 saw the implementation of the Minimum Energy Efficiency Standards (MEES) legislation and we are committed to meeting our net zero ambitions for our buildings. We will continue to work with our tenants to improve and enhance our estate wherever possible by exploiting central government grant funding.

The breadth of our portfolio, which is wholly invested in the local area, alongside a strategy that is underpinned by robust governance and strong risk management, has enabled us to maintain a solid revenue returns and capital yield year-on-year. Our future strategy is not governed solely by revenue or yield, rather, it is activity-focussed across a range of areas, to optimise returns, maintain good quality stock, and improve the covenant quality of tenants, whilst providing a range of accommodation to support local businesses, small and large, established and new.

After a year of stabilisation and resilient performance, our promise remains steadfast in that we will continue to proactively manage our portfolio, its suitability and performance, as well as its financial returns – including considering the wider financial challenges faced by local government under the backdrop of a reduction in central government funding over the last decade. Our strategic focus will remain on continuing to achieve greater yields from our investment portfolio or dispose of low yielding assets where yield growth is not achievable.

We will continue to integrate our Environmental, Social and Governance (ESG) considerations to our investment and management activity, ensuring that our portfolio remains both stable and sustainable, now, and into the future.

Richard Sword
Strategic Director for City Development and Neighbourhoods

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By Tarrant Parsons -Senior Economist at the RICS.

Notes:

As one of the UK's largest local authority and charity fund managers, the CCLA manages investments for the public sector, charities, and religious organisations. Investments include the Local Authorities Property Fund that aims to provide investors with a high level of income and long-term capital appreciation.