

Investing in Leicestershire Programme

ANNUAL PERFORMANCE REPORT
2024 - 2025



INTRODUCTION

The Council first established an investment portfolio in 2014 with a view to it generating additional funding to improve financial resilience thereby supporting the continued delivery of essential quality frontline services.

From an initial investment of £15 million together with the industrial and farms properties held by the Council (valued at £40 million in 2014) the portfolio has grown to its current value of £292 million by the investment of a further £149 million in both direct and non-property investments , including a number developed on sites held by the fund.

In 2023 the fund was rebranded as the Investing in Leicestershire Programme (IILP) adopting its current strategy of focussing future investment in areas that addressed social and economic market failure whilst continuing to maximise financial returns from its assets.

The management of the portfolio is overseen by an Advisory Board and as part of its agreed governance an Annual Performance Report is produced each year. This the eleventh annual report sets out the overall performance of the IILP during the 2024-25 financial year providing details of its current investments and in respect of the direct property portfolio a detailed comparison with the wider real estate investment market. Further it reviews progress in respect of major projects and the future potential of the portfolio to enable the continued delivery of an ongoing income stream and capital receipts vital to the delivery of frontline services whilst continuing to support job creation and economic growth across Leicestershire



SUMMARY

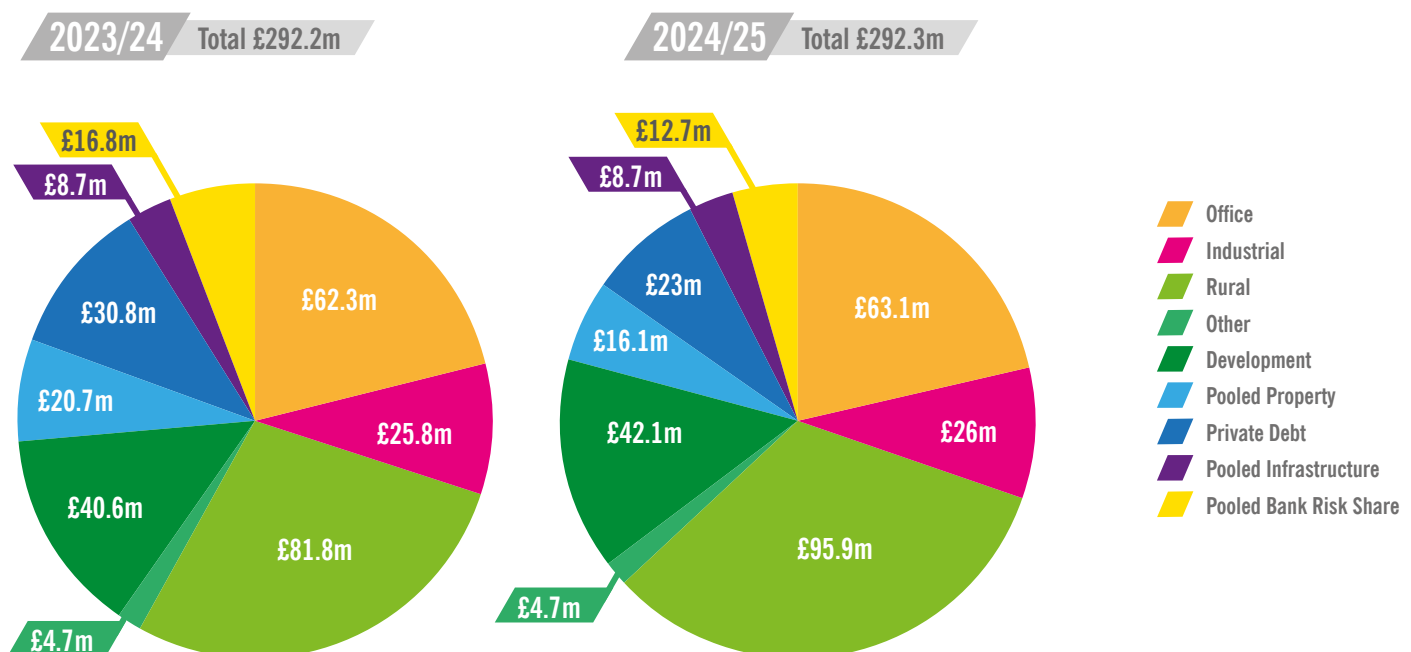
This report forms the annual review of the Investing in Leicestershire Programme (IILP) portfolio, reporting on performance for the year to 31st March 2025.

The IILP has continued to contribute to the economic, social, and environmental wellbeing of the people of Leicestershire; making a significant contribution to the Council's Strategic Plan. The income generated by investment in high quality assets provides increased financial resilience and underpins the Council's ability to deliver a comprehensive range of quality services now and in the future.

The annual report examines the development and performance of the overall portfolio, the potential of the future investment programme to deliver enhanced returns and the outlook for the wider investment market and how it might impact on the future investment strategy.

TOTAL VALUE BY SECTOR (as of 31st March 2024)

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As of 31st March 2025, the capital value of the portfolio, including the let areas of County Hall (currently managed alongside the portfolio), totalled £292.3 million compared with the value as of 31st March 2024 of £292.2 million. The opening and closing valuations were calculated based on a combination of internal and external asset valuations, with external valuations being undertaken in 2024-25 for the entire direct portfolio.

Looking ahead, the IILP is well-positioned to capitalise on emerging opportunities and deliver enhanced returns. Our strategic focus will remain on sustainable investments that drive economic growth, social development, and environmental sustainability.

Financial summary

	Value on 31st March 2024 (£m)	Transactions			Valuation Change (£m)	Value on 31st March 2025 (£m)	Net Income (£m)
		Acquisitions (£m)	Net Capital spend (£m)	Sales & Transfers (£m)			
Office inc County Hall	62.3		0.2		0.5	63.1	3.8
Industrial and Distribution	25.8				0.2	26.0	1.2
Rural	81.8				14.1	95.9	0.1
Other Property	4.7					4.7	0.2
Sub-Total Managed Property	174.7		0.2		14.8	189.7	5.4
Development	40.6		2.0		(0.5)	42.1	(0.3)
Direct property	215.3		2.3		14.3	231.8	5.2
Pooled Property	20.7			(5.1)	0.5	16.1	0.7
Private Debt	30.8		1.2	(6.2)	0.4	23.0	1.6
Pooled Infrastructure	8.7					8.7	0.5
Pooled Bank Risk Share	16.8			(2.5)	(1.6)	12.7	3.4
Total Diversifiers	77.0		1.2	(13.8)	(3.8)	60.5	6.2
Total	292.2		3.5	(13.8)	10.5	292.3	11.4
Additional Central Charges							(2.8)
Overall Total	292.2		3.5	(13.8)	10.5	292.3	8.6

Notes: (i) All figures are rounded to nearest 0.1m. (ii) Opening valuation figure adjusted to include the valuation of the let areas of County Hall managed in conjunction with direct property portfolio since 2023.

As of 31st March 2025, the Programme held managed direct property assets of £189.7m, including the let parts of County Hall and development property of £42.1m; a total of £231.8m representing an increase of £16.6m on the previous year. The majority of this increase is attributed to the uplift in the value of the rural estate due to the generation of “hope” value, i.e. the potential increase in the value of the estate is based on the expectation of future development or changes in use.

The portfolio also includes external pooled property funds, private debt investments, pooled infrastructure funds and pooled bank share funds, collectively referred to as the ‘diversifiers’. The diversifiers have a total value of £60.5m, a decrease of £16.5m from 2023-24, largely as a result of capital repayments and disposals amounting to £14.9m.

The direct property portfolio delivered a strong return of 9.5%, outperforming the broader market's 7.7% Capital growth, underpinned continuing increase in hope value within the rural sector as the pipeline of potential development sites progress through the planning system, showed an increase of 6.6% compared to just 1.8% in the market. With the exception of industrial and distribution sectors, the other sectors compared very favourably with the wider market. The initial hardening of the market in the second half of the year was not reflected in the valuation. Consequently, the mid-year valuation timing caused a mismatch in capital values, as it did not reflect the market's subsequent rise later in the year. This led to differences in yield and valuation trends. However, as the market stabilises, these effects are balancing out, therefore while industrial assets showed lower growth this year, future performance is expected to align more closely with the market.

In addition to the normal sinking fund provision (central charge) that is applied to revenue in line with previous years, an additional charge of £2.8m has been made in the 2024-25 year in order to assist in meeting the sinking fund's target level. This charge recognises the prudence of building a provision for future maintenance or unforeseen costs. A sinking fund can be thought of as a savings account or contingency fund which ensures that there are funds set aside to cover one-off expenses required in the future to maintain the assets' capital value.

The LiLP also recognises potential bad debts and accounts for these in each financial year in line with the Councils policy for late payment for invoices. Once a bad debt provision is established by charging the profit and loss it is reassessed each year based on outstanding monies still to be received. The value held as a bad debt provision may fluctuate as income is received to clear debtor accounts. The assessment at the end of 2024/25 was that the provision did not need to be increased.

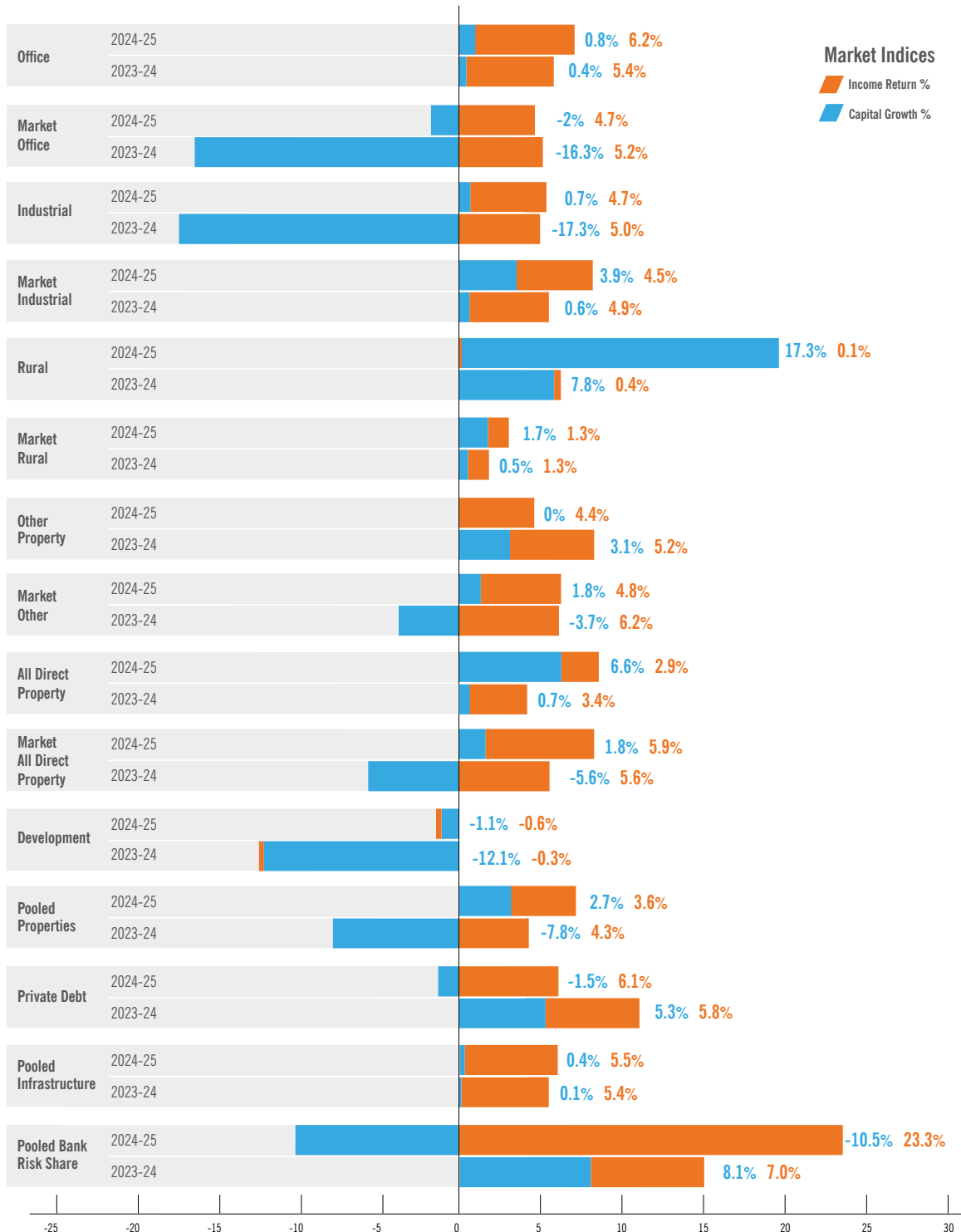
Net income also takes account of centrally incurred costs which are allocated to the main direct property sectors. These costs include employee costs, bad debt provisions and sinking fund contributions. The current target level for the sinking fund, to be built up over the period to 2027/28, is set at approximately £6m. This will be reassessed each year based on information regarding the assets within the Fund.

The net income from the direct property portfolio was £5.2m for the year. Together with the income from diversified investments, the total net income was £8.6 million, compared to £7.6 million in the previous year. The current year benefited from higher-than-expected income from the bank risk share investments within the diversifiers. For the year ended, the total portfolio generated a net income return of 2.9%, compared to 3.3% in the previous year. Excluding the Development and Rural assets, which are predominantly held for capital returns rather than revenue income, the equivalent figures are 5.4%.



PERFORMANCE AND COMPARISON AGAINST INDUSTRY BENCHMARK

PROGRAMME Performance



The Programme's benchmark is the "All Property" total return (capital growth plus income return) of the market benchmark monthly index. The total return for the portfolio for the year to 31st March 2025 was 9.5% compared to the target level of 6%.

The managed direct properties produced a total return of 11.6% which is well above both target and the market level of 7.7%. Importantly the fact that the property portfolio continues to be valued at 1st October each year will result in the assessment of the portfolios performance not being fully aligned with its benchmark, as the impact of yield changes in the second half of each year are not being reflected in values until the following year. Whilst the effect of this counterbalances over the longer term, as demonstrated by the returns over a 5-year period, at times of economic and market turbulence comparison with the market is difficult to assess accurately.

Accordingly, the managed direct property portfolio achieved an increase of 6.1% on the 2023-2024 year driven by higher than anticipated capital growth within the rural sector without which the managed direct property sectors would have achieved parity with the market.

- The office sector continues to perform consistently well against the market benchmark. Whilst producing a small capital growth of 0.8%, income return also outperformed the market at 6.2% delivering an overall return of 7.0% significantly better than the market return of 2.7% which continued to include negative capital growth with market values falling a total of more than 30% over the three year period of market correction. Net income rose by £0.3m to £3.2m over the year due largely to maintaining near full occupation of the major office assets.
- The returns from the combined industrial and distribution sectors were 5.4% compared with the previous year at minus 12.3%. Whilst capital growth remained constrained at 0.7% against a market level 3.9% due in part to the nature of the properties within the portfolio values now appear to be stabilising following the market corrections of late 2022 and 2023. However, the income return of 4.7% aligned with market levels.
- The rural sector achieved an overall return of 17.4% in 2024-2025 compared to the market level of 3.0%. Whilst the income return of 0.1%, impacted by the changes in valuation methodology introduced in 2022, and a substantial contribution towards the sinking fund, was again below the market level of 1.3%, capital growth of 17.3% accrued as the value of land within the future development pipeline increased in value reflecting its future development potential. Agricultural land prices are by their nature less volatile than other sectors, however, in recent years there has been strong growth in freehold values over the year as a result of investors recognising that it represents a "safe haven". This trend has slowed and with an increased supply prices have stabilised.
- The small alternative or other property sector produced a return of 4.4% slightly below market levels. However, the sector provides a stable income; the portfolio holding a mixed range of assets within this sector, including a car dealership in Leicester city, a petrol filling station in Loughborough and a supported education school which overall makes it less vulnerable to market volatility.



- The performance of the development sector showed a significant improvement on 2024-25 but still delivered a negative return of minus 1.7% compared to the previous year when economic conditions caused the market correction experienced by other sectors resulting in an overall negative return of minus 12.4%. The Lutterworth East development site remains the single most valuable asset within the development portfolio. Whilst capable of achieving significant capital growth, development properties are unlikely to generate than nominal income during the development phase. It is therefore normal that the cost of planning and promoting schemes will exceed any income received and consequently an anticipated small revenue loss resulted in an income return of minus 0.6%. It is anticipated that the sector will show positive returns as in future years as further developments are completed and other sites brought forward for disposal with the benefit of planning permission thereby generating either rental income or capital receipts.
- The pooled property investments are spread across four separate investment managers. A total of £25m was invested between 2015 and 2019. A 3.6% income return was welcome and ahead of budget, capital values across the pooled property estate did firm up over the year with a £0.5m increase after the fall in capital values experienced during the previous year when the effect of rising interest rates fed through to property valuations which had already suffered in the previous year when Bank of England base rates rose from 0.75% in April 2022 to 4.25% by March 2023.
- The Lothbury property unit trust, one of the four pooled property funds is still in the process of being wound up with the majority of the holdings having been sold and capital returned to investors following an Extraordinary General Meeting (EGM) on the 28 March 2024. For clarity it is important to note that this winding up of a property fund is a forced sale over a period when property values have been depressed in comparison to the periods preceding the increase in the Bank of England's base rates. The forced nature of the sales means the liLP fund is not able to 'hold' the investment, collect the income and then choose when to exit. The overall expected capital loss (invested capital minus returned capital from asset sales) is expected to be £1.8m based on capital received to date and current valuation of the remaining assets. The total return including quarterly income distributions shows a positive return since inception, +0.4% (IRR, internal rate of return)
- The Fund invests in the Private Debt asset class via one institutional manager. The liLP has invested over a number of years in three different vehicles, starting with £20million in 2018 with further commitments being made in 2021 and 2023 to maintain exposure to this asset class as capital is returned. Private debt income returns were ahead of expectations in the year benefiting from the higher base interest rates that the underlying loans are linked to. The since inception internal rate of return (IRR) for three private debt investments were 5.1%, 6.6% and 9.6% respectively.



- The infrastructure investment is made via one manager. This is a globally diversified infrastructure fund investing in core assets. The assets are operational and provide a defensive focus. Investments in critical assets which are underpinned by long term contracts, supported by regulation in many cases and situated in developed markets are favoured. The in year net income was ahead of expectations. The Fund is denominated in USD with the quarterly income converted to GBP when received and carrying value translated to GBP. The carrying value of the investment in GBP is £8.7m and generated £0.5m income in 2024/25.
- The Fund has also invested in a bank risk share strategy in 2022/23. The total £15m was fully called by the manager by December 2022 with distributions commencing in January 2023. Income received during 2024/25 continued to be higher than originally expected due to the continued higher underlying bank base rates and the favourable market conditions when the manager was completing deals in 2022/23 which led to better priced deals. The interest rate conditions over the last two years which were unfavourable (higher for longer bank interest rates) for many investment sectors have been a positive for this diversifying investment. A net income of £3.4m was received in the year, well ahead of expectations. The excess net income for the liLP compared to the budget allowed for a sizeable acceleration in the build up of the sinking fund during the year. This investment, which has a fixed life has also started returning capital and work is underway to replace the exposure subject to approvals.
- Diversifier investments had a net return of capital in the year of £12.7m reflecting the return of capital from pooled property and private debt investments. The exposure to diversifiers has reduced as a percentage of the total liLP portfolio as a result over the year from the target allocation of one third. Plans are in place to replace diversifier exposure through 2025/26.



ANNUALISED RETURNS

Total Direct Property Portfolio

	2024-25	3 year	5 year
Net Income Return	2.9%	3.6%	3.6%
Capital Growth	6.6%	12.9%	10.4%
Total Return	9.5%	16.5%	14.0%
Total Market Return	7.7%	3.5%	4.4%

As the liLP has now been in operation for several years, the data for returns over the longer period better demonstrates the stability of the returns achieved by the assets in the portfolio by reducing the visible impact of any in-year peaks or troughs in performance.

Over the 3 year period including 2024/25, the total return of 16.5% was achieved against the market 3 year annualised returns of 3.5%; over 5 years, the market returns were slightly better at 4.4% still below that achieved by the liLP at 14.0%.

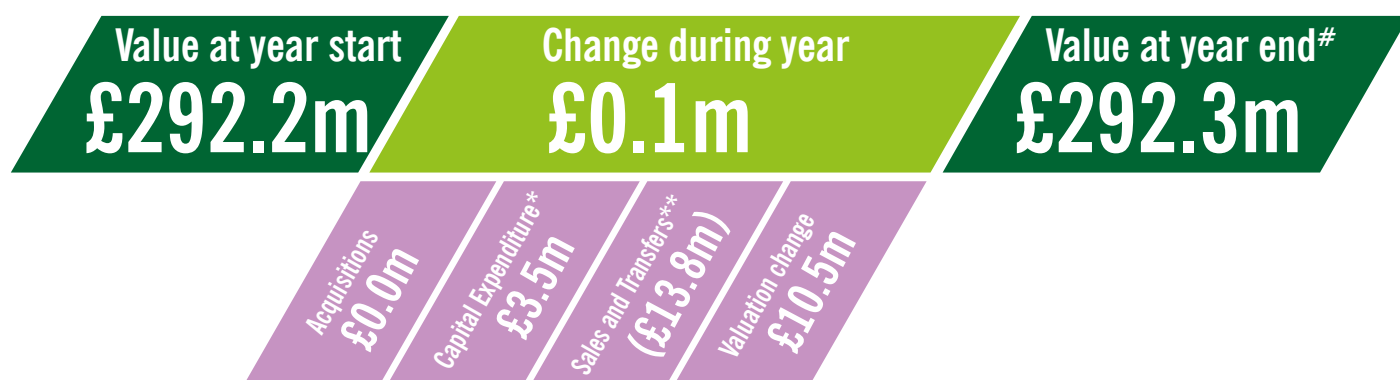
If the effect of the valuation methodology change within the rural sector in 23/24 is excluded, the total market returns still outperforms the market by a significant margin, at 6.4% over 3 years and 7.8% over 5 years.



CHANGES TO THE PORTFOLIO DURING THE YEAR

Summary of Changes

During the year, the value of the portfolio, including the value of the let areas of County Hall, increased slightly from £292.2m as at 31st March 2024 to £292.3m as at 31st March 2025; the chart below setting out details of transactions and changes in valuation.



[#]Direct portfolio properties valued as at 1st October 2024.

*This includes spend on farm estate buildings and the office and industrial properties.

** This sum is solely return of capital to the fund from diversified investments.



TRANSACTIONS THROUGH THE YEAR

Direct property acquisitions

There were no property acquisitions during the year.

Property Disposals

No property disposals were completed during the year. However, agreed sales to the value of £9.6m were carried over into future years of which £5.1m is due to be received in the current 25/26 financial year.

Property Transfers

No direct property transfers have been made during the year.

Diversifiers

No new diversifier investments were entered into during 2024/25. However, past investments in pooled property, private credit and bank risk share were returning capital throughout the year. In order to meet the investment strategy of holding around a third of total assets within diversifiers new commitments are planned pending formal due diligence and approval.

Pooled Property

One of the four pooled property funds, Lothbury property unit trust was being wound down during 2024/25, as a result the lilP received £5.0m from property sales conducted by the manager. The Fund expects to receive the remaining capital during 2025/26.



PORTFOLIO REVIEW

Yield

The yield from the direct managed portfolio is 4.5% (4.0% in 2023) somewhat below the market benchmark national figure of 5.6%; the portfolio's overall yield being impacted by a low yield from the development assets which has a disproportionate sector weighting compared to other portfolios meaning that overall, the portfolio will likely always fall just below the benchmark until such time as those developments are completed and become income generating or are released from the portfolio.

Sector Proportions

With no direct property transactions during the year only movements in value, particularly in respect of the rural sector, have resulted in further shifts in the sector weightings as illustrated earlier in the report. However, the reduction in the value of the Diversifier portfolio has resulted in a shift in the balance between the two areas of investment with direct property increasing from 73% to 79%; the previous weighting between the two being considered appropriate in the Hymans Robertson Report of January 2024.

In relation to the direct property portfolio the long-term aim is to maintain a balance between sectors that reduces risk and maximises the potential for achieving financial resilience in the shorter term. In considering future acquisitions, the Programme will continue to focus any property purchases on assets that address market failure and provide wider economic and community benefits and the capability of contributing to the achievement of the County Council's strategic goals as well as delivering a long-term income stream, as set out in the IILP Strategy.

Rent Reviews, Lease Expiries and Tenant Only Breaks

During 24/25 there were 10 rent reviews, 32 lease expiries and 11 tenant-only break options which fell due across the commercial property portfolio, of which one related to an asset earning in excess of £30k per annum; of these 10 rent reviews were concluded in the year, together with 6 lease renewals and 15 new lettings. Thirteen leases terminated during that timeframe and of these 8 units are currently being marketed, with the other 5 having been relet promptly. Consequently, whilst the vacancy rate increased slightly, the overall rent roll for the portfolio rose by £215k p.a. The negotiation of rent reviews and lease renewals forms part of normal day-to-day property management, however the particular circumstances of individual leases means that it is not always appropriate to action these immediately they fall due.

Following on from rent review notices served in respect of farm tenancies, 35 reviews have been agreed, with a further 4 remaining to be concluded. The total rental uplift across these agreements is £73,000 per annum (equating to 17% uplift overall).

New Major Lettings

Over the 2024/25 year the following major new letting(s) or pre-lets were achieved:

Ground Floor, Building 2, Lichfield. Following the departure of the tenant in April 2024 a settlement was agreed in respect of dilapidations and a refurbishment program proposed which included for the subdivision of the building into two self-contained units; ground and first floor.

New tenants were secured for the ground floor with occupation to commence following the completion of the refurbishment. An agreement for lease was entered into in June 2024 with the new lease commencing in July 2025 following the completion of the works. The passing rent is £159,633pa.

Future Investments

During 2024/25 funding of £62m was made available through the Medium-Term Financial Strategy (MTFS) 2024-2028 for additional investment. These funds were committed to the delivery of the following developments that will have the effect of further transforming the portfolio, achieving target rates of return, delivering additional income, and contributing to the realisation of wider strategic goals.

Leaders Farm South, Lutterworth

Background

This site formed part of the County Farms portfolio and was identified as having possible office and industrial development potential some years ago.

Following extensive marketing of the site demand has been identified for roadside and storage uses.

Two major roadside food and drink retailers expressed an interest in a parcel of land, extending to 1.6 acres at the north-western corner of the site. Whilst a departure from the Local Plan, because of a lack of demand for the Class B1 – office uses, the prospective tenants have been successful in securing planning permission for the proposed drive through units.

The drive-through units will generate an income of £190k pa. The planning consent required some s.278 highway works. A contractor has been procured to build the new units. It is anticipated that the works will commence Q3 2025

The future development of the balance of the 6.1-acre site is now being reviewed. There is interest for Light industrial/ Distribution use. However, this would be a departure from the current local plan. If the County Council is successful in obtaining planning for the employment units, they are projected to generate a rental income of circa. £550k pa. The overall construction cost is projected to be in the region of £6m (excluding the £2.5m already spent on the estate roads and services) giving an expected income return of c.6.2%.



Airfield Farm Business Park (Third & Final Phase)

Background

Following completion and the successful launch of Phase 2 of the new industrial development at Airfield Farm Business Park, planning consent was granted in July 2024 and building began in December 2024 for a 105,794 sq. ft. development on 7.69 acres of the site; 102,194 sq. ft for E class light industrial units (formerly known as B1 use) and 3,600 sq. ft for two Drive-thru units (Sui Generis). The layout incorporates a 60,000 sq. ft unit, a 14,000 sq. ft, two Drive-thru units, EV Charging bays and a range of starter and grow on units of between 1,500 sq. ft and 10,000 sq. ft being those elements of the original proposal for which there is a strong market demand and remain viable.

A pre let agreement has been completed for the 60,000 sq. ft unit. Other units totalling 19,000 sq. ft are under offer, as are one of the Drive Thru units and the EV Charging bays.



Solar Farm Development, Quorn

Background

The proposal, approved in 2024, sets out plans for a 10MW solar farm on County Farms land at Quorn. Over the past year, various delivery options were considered. Due to limited resources and the need to comply with planning consent and meet the grid connection deadline, the opportunity was marketed for a freehold sale. The sale was successfully completed in April 2025, and the new owner has now implemented the planning consent and aims to have the solar farm up and running by the end of the year, with the balance of the capital receipt payable on connection to the electricity grid.

Development Sites

The Fund holds a number of assets within the portfolio that have been expressly retained or purchased with a view to realising their development potential in order to realise capital receipts or wider finance benefits to support the Council's capital and revenue programmes.

Lutterworth East

The allocation of the East of Lutterworth SDA comprising 2,750 dwellings, 23 hectares of B1, B2 and B8 employment land, a community hub, two primary schools, 110 hectares of open space including a country park together with substantial highways infrastructure was secured as part of the Harborough Local Plan which was adopted on 30th April 2019.

A hybrid planning application (in outline for the residential and commercial development and in detail for the spine road and other highways infrastructure works) was considered by Harborough District Council's Planning Committee on 28th July 2020. The planning committee resolved to grant planning permission subject to conditions and the completion of a section 106 Planning Agreement.

The Section 106 Agreement was completed, and the decision notice issued on 17th May 2022, however, University Hospital Leicester lodged an application to seek a judicial review of the district council's decision. After an appeal, their challenge was dismissed.

A review of the site was undertaken in 2024, with some initial soft market testing, recognising how the context for the proposed development has changed since the application was submitted in 2019. The impact of COVID on where people work (less office space needed) and escalating costs due to build cost price inflation as well as the lack of grant funding. This has made the scheme challenging to the market to deliver in its current form due to the high levels of upfront infrastructure costs of approximately £140m required to bring the scheme forward.

As a result of this work a viability assessment was submitted to Harborough District Council providing a case to reduce the percentage of affordable homes on the site in order to improve the schemes viability. Productive discussions took place with the planning officers at Harborough District Council in order to find a way forward to improve the scheme's viability and to ensure that the district benefits from the delivery of houses that it had provided for in its Local Plan. Subsequently two applications were submitted to Harborough District Council. The applications focused on the review of the level of affordable housing, being reduced to a minimum of 10% (subject to a viability assessment on each of the four residential phases) and the size restrictions on the B8 units to the south of the site.

These applications were approved at the planning committee (3rd December 2024) and have significantly improved the sites viability. It is anticipated that the southern area of the site, designated for B8 distribution, will be offered for sale to the market in the final quarter of this year. This will provide capital income that will facilitate the initial phase of the highway's infrastructure making the residential site more attractive to potential delivery partners.



M69 Junction 2 – Stoney Stanton

Following the Cabinet decision in March 2020, work has been progressed on the promotion of 103 acres of County Council land as part of a larger residential-led mixed-use development of up to 5,000 houses. Working in collaboration with other landowners and their developer partners, submissions have been made to Blaby District Council's 'Call for Sites and Issues and Options' consultation and work is ongoing to provide the necessary evidence base to support the sites allocation as part of the emerging Blaby District Local Plan.

The local plan process has been significantly delayed with the result that the Regulation 19 Pre-Submission consultation is not now likely to take place until the end of 2025 pushing the likely date of adoption back to 2027. Subject to the scheme being included as a proposed allocation in the Pre-Submission Draft, it is currently proposed that an outline planning application be submitted in advance of the Examination in Public. The timing of surveys and site investigations is now being geared to the revised timetable with an Environmental Impact Assessment Scoping Request submitted to Blaby District Council in June this year.

In addition, following negotiations with Stoney Stanton Parish Council a land exchange has been agreed which secures the land necessary to provide highway improvements that will divert traffic away from the village centres of Stoney Stanton and Sapcote and provides the parish with additional playing fields and informal open space.

Throughout the process, the Landowner Consortium has engaged with Blaby District Council, key stakeholders, and the local community, including the establishment of a community liaison group the feedback from which is being used to help shape the master planning of the scheme.

Other potential sites

A further pipeline of development sites is being brought forward on an ongoing basis largely through the local plan process, by their submission to Call for Sites consultations at the start of the plan review process and thereafter by making appropriate responses to the further consultations. By securing future local plan allocations, investment returns, and a stream of capital receipts will be maintained.

In addition to potential residential and employment opportunities, sites with potential to support the delivery renewable energy infrastructure or biodiversity gains are also being identified and could potentially form an integral part of the pipeline of future sites.

Voids

Despite leasing over 42,801 sq. ft. of office and industrial space during the year, the level of unoccupied units increased by 16,529 sq. ft. illustrating the continued turnover of units, with less space being leased out than returned by tenants. The overall voids level across the portfolio in 2024-25 was 5.6% (40,623 sq. ft. in 25 units) of core direct net floor area.

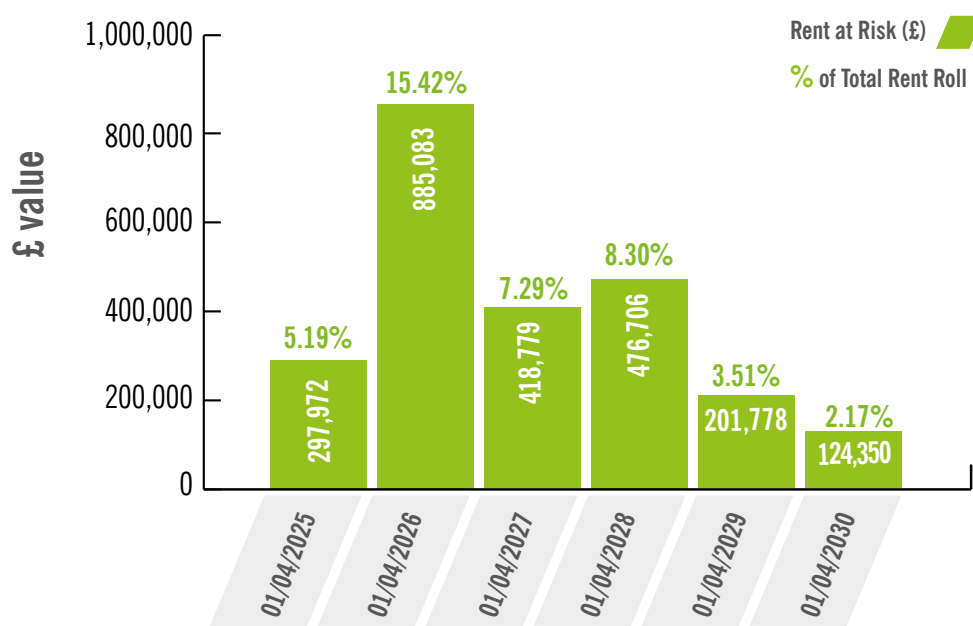
Continued strong demand for leases continues to suggest that the relatively low level of voids can be maintained.

Rent Arrears (Direct Portfolio)

As of 31st March 2025, total 90-day debt amounted to £981,000, equating to 11.1% of gross portfolio income, a fall of £60k (5.7%) on the previous year and although systemic debt, which is taken into account in determining the level of funding held in the bad debt provision, remains higher than desirable having built up over several years, rent collection remains in line with wider industry performance especially during the ongoing turbulent economic conditions with over 86% of rural rents and 82% of industrial and office rents collected on time for Q4. Payment of all outstanding debts is being actively pursued through debt management procedures. Further, no debt is written off until such time as all avenues including court action have been fully exhausted which account for its current level.

Lease Expiry Profile (Direct Portfolio)

The table below illustrates the profile of rents receivable from leases expiring in each year within the portfolio over the next 7 years both in terms of rental value and a proportion of total rental income. Where a tenant has an option to break within a lease, the worst-case scenario that the tenant will exercise such an option is assumed, whereas in practice it is likely that not every tenant will elect to do so.



The largest figure in the table above, and presenting the greatest risk to the portfolio, relates to the 2026 financial year when two leases at Embankment House, Nottingham and 6 of the 17 leases at Apollo Court, Coalville expire. In accordance with usual practice, a policy of early engagement with tenants is pursued with a view to agreeing lease renewals in advance of the termination date.

PROPERTY INVESTMENT MARKET REVIEW

Economic Conditions¹

UK gross domestic product (GDP) is estimated to have grown by 0.7% in Quarter 1 (Jan to Mar) 2025, with a further rise of 0.3% in Quarter 2 (Apr to June), unrevised from the first estimate. In output terms, growth in Quarter 2 2025 was driven by an increase in the services and construction sectors, however production fell by 0.3%. In expenditure terms, growth in the latest quarter was driven by increases in gross fixed capital formation, net trade and household consumption. However, monthly real gross domestic product (GDP) is estimated to have fallen by 0.1% in May 2025, following a fall of 0.3% in April 2025 leading to fears that the economy will have shrunk in Q2 2025.

The unemployment rate stood at 4.7% at the end of Q2, up from 4.3% a year ago whilst the number of job vacancies and people employed continues to decline. In addition, at 5.6%, regular wage growth remains stubbornly high.

CPI inflation rose to a 18-month high of 3.8% in July and is expected to remain above the Bank of England 2% target until at least 2026. House prices and rents continue to rise while mortgage rates have fallen slightly over the past few months. The combination of expected economic weakness, above-target inflation and strong wage growth leaves the Bank of England in a difficult position, suggesting it will continue with its gradual approach to cutting interest rates; the Bank Rate currently standing at 4.25%.

Economic Outlook

Latest HM Treasury consensus forecasts predict growth of 1% this year and 1.1% in 2026. The IMF is more optimistic and believe UK GDP growth will improve from 1.2% this year to 1.4% in 2026.

¹ The information contained in this section of the report has been sourced from published central government data and research documents and news releases published by leading property agents including Colliers International, Savills and Lambert Smith Hampton.

Investment Market

While some European markets have recorded an increase in investment volumes in Q1 2025, the UK witnessed a decline from £16.1bn in Q4 2024 to £9bn and was 36% below the five-year quarterly average. The Q1 figure marked the weakest quarterly total since Q4 2023 and affected all the regional markets across England whilst Scottish markets saw a modest increase in investment. The most sought-after sector was offices, accounting for 25% of all investment volumes. Apartments including PBSA (21%), industrial (19%), retail (15%), and hotels (6%) follow. Despite the weak start to the year there are some signs the investment market that the investment market will show an improvement in H2 2025.

Property capital values have continued to recover as equivalent yields fell for the second consecutive quarter during Q1 2025 following ten consecutive quarters of increases.

Property Market Forecasts

The outlook for the commercial real estate sector remains uncertain. However, rising capital values, less restrictive access to commercial finance, optimism in the latest market survey results and further anticipated interest rate cuts all indicate that the conditions exist to deliver a sustained recovery. Nevertheless, it is still anticipated that annual investment volumes in 2025 could still be below those of with the uplift coming in 2026. Whilst interest rates may end the year at 3.75% the potential for yield compression will be constrained by the lack of movement in gilt yields which are not expected to move significantly this year. At the All-Property level, forecasts predict that equivalent yields will fall by 0.25% over the year to 6.37% with further moderate declines expected over the remainder of the period to 2029. The property yield/gilt spread narrowed to a 17-year low of 2% in 2024 and it is considered possible that contract further in 2025 before widening again in 2026.



The recovery in capital values is likely to be modest by historical standards, with growth of 5% expected in 2025 before slowing over the following 4 years with anticipated growth over the period to 2029 averaging 3.4% per annum. Sustained positive income returns and an improvement in capital values will result in positive total returns growth of 9.8% at the All-Property level in 2025, before reducing to 8.4% in both 2026 and 2027 reflecting the slowing in capital growth. Over the period from 2025 to 2029 Shopping Centres (10.9% per annum) and Retail Warehouses (9.4% per annum) will see the strongest growth in total returns as a result of solid income returns.

It is predicted that investment volumes are likely to remain weak in the coming months with liquidity in the market only returning as interest rates and debt costs reduce further. With a slowdown in construction activity coupled with signs of downward pressure on vacancy rates and sustained rental growth for prime assets the office market should become more attractive. There are indications that yields have started to stabilise across most sub-markets, but it is considered that yield compression will be constrained due to debt costs remaining higher for longer than originally forecast. However, as initial market data for Q1 2025 show significant yield shifts it is predicted that yields will fall by 0.35% in 2025. Thereafter, it is expected that yields will continue to slowly compress further over the next few years. Prime rents should see further rises due to the now more limited supply of high-quality space. However, secondary and lower quality office rents are likely to see very limited growth. Forecasts predict that average rents across all offices will increase by between 2.5% and 3% in 2025, before slowing to 2.2% and 2% in subsequent years.

Total returns across the office sector are predicted to be 7.7% in 2025 as capital values recover and are forecast to average 6.7% pa over the period to 2029.

Industrial investment volumes fell markedly over Q1 2025 and at £1.7bn were 50% below the 5-yearly quarterly average. Average yields appear to have stabilised but remain nearly 2% above 2022 levels. Currently most investors are targeting Core+ and Value-Add strategies, focusing on assets offering near-term reversion, whether through rental growth or asset repositioning, particularly for assets located in prime locations. In general, the sector performance is improving and forecasts suggest that total returns will be in excess of 10% this year, moderating to around 8% in 2026. As is the case with all the other sectors, yield compression will be somewhat limited as borrowing costs remain higher for longer than previously anticipated. Occupier demand is currently much reduced as companies delay expansion plans amid economic and geopolitical uncertainty; demand focusing mainly on high quality new build space. This has resulted in an increased level of available space and a consequent fall in the level of new starts stabilising the market over the next year.

Rents are forecast continue to rising over the next 5 years although the rate of growth will slow further falling to between 3% and 4% per annum from the exceptionally strong rates recorded during 2021 and 2022.

In common with other sectors quarterly investment volumes across the retail sector slowed in the Q1 2025 from the Q4 2024 three-year high of £3bn with total transactions 30% below the five-year quarterly average of £2bn. Retail parks continue to be in high demand with the potential for further yield compression following reported falls of 0.35% over the past 12 months and a further modest reduction in Q1 2025.



Despite unfavourable economic conditions a modest increase in retail sales is predicted for 2025 and with online sales stabilising at 2023 levels physical shopping still accounts for over 70% of the market.

However, with a number of significant retailers going into administration releasing a large number of properties to the market data for Q1 shows vacancy rates across high street shops rose with retail warehouses and supermarkets recording record or near-record vacancy rates although shopping centres experienced an increased take up of space.

The market readjustment that led to negative rental growth in the years between 2018 and 2022 meant that All Retail rents have risen at their highest rate since 2005 over the past 2 years.

It is expected that retailers will continue to re-focus on physical stores for the immediate future resulting in rental growth at the all-sector level accelerating from 2% in 2024 to 2.7% in 2025 with. Standard Retail – Central London (+4.5% pa) and Retail Warehouses (3% pa) seeing the strongest growth over the 2025-2029 forecast horizon. With strong income returns and solid capital growth All Retail total returns are expected to be c. 12% in 2025, driven by Retail Warehouses at an estimated 13.5%. Total returns are then expected to stabilise at around 8% per annum.

Rural Property remains a safe haven for investors. Income returns of c.1.3% are forecast to be maintained over the period to 2029. Although subject to regional variations overall modest increases in capital values are forecast to be maintained over the period to 2029 following an initial period of readjustment in the current year; the focus on properties offering further long term capital growth through the realisation of development potential. However, following the increased supplies of land on the market in 2024, as a result of investors moving back into other sectors or forced sales as farmers faced increasing financial pressures, the supply has significantly fallen in H1 2025 as the farming industry takes stock following the IHT reforms thereby stabilising the market.

Sales volumes and the general performance of the alternative sector in 2024 mirrored that of the market generally; a trend that has continued into 2025. The investment market in this sector has generally been subdued being affected like the other sectors from the weak economic outlook, combined with higher than anticipated interest rates and the slower than expected fall in the cost of debt. The strong demand for investments in segments such as student accommodation which peaked in H1 2022 has declined sharply since with the level of transactions in Q1 2025 remaining below the 5-year quarterly average. Following the increase in yields of more than 1% over the period since H2 2022 rates have now stabilised providing the prospect of future capital growth which coupled with strong income returns will deliver positive overall returns.

In common with the market in general it would appear that the market for pooled property investments is also beginning to stabilise following significant falls in value and negative returns over recent years. However, the level of returns going forward are likely to remain modest even as the wider economy recovers making other alternative investments more attractive.

Investment Strategy Update

The Portfolio Management Strategy for 2025 to 2029 is aimed at supporting the development of the Portfolio to further enhance its contribution to the delivery of strategic goals whilst continuing to improve the Council's financial resilience as demand on services and operating costs continue to rise. It outlines how the Council will look to direct investments during this period developing the Portfolio to address areas of specific economic or social market failure and how it will manage these to help achieve the strategic priorities of the Council.

The Strategy is an integral part of the Council's Medium-Term Financial Strategy (MTFS) and intrinsically linked with the Corporate Asset Management Plan (CAMP) and the Treasury Management Strategy and Annual Investment Strategy and it should be read in conjunction with these documents.

The specific aims of this Strategy are to ensure investments funded or held in the Portfolio:

- Support the objectives of the Council's MTFS, Corporate Asset Management Plan, Strategic Plan, its Economic Growth Plan, and the County-wide Local Industrial Strategy.
- Support growth in the county and its economic area of influence and ensure there is a more diverse range of properties and land assets available to meet the aims of economic development.
- Maximise returns on Council owned property assets.
- Supports the delivery of front-line services through increased income generation from existing investments, or through capital investments that will reduce operating costs.
- Maintain a diverse portfolio of energy efficient and sustainable direct property and other investment assets which support economic growth and environmental sustainability.
- Support the Council's strategic objectives by working with partners to maintain momentum in the development of strategic sites and renewing existing employment sites and premises where there is demand thereby addressing areas of market failure.
- Contribute towards the development and implementation of a Net Zero Carbon 2030 Plan for the Council by reducing demand for energy and increasing the generation and use of renewable energy.
- Channelling new investment into schemes that:
- Maximise the potential to address economic and social market failure.
- Improve property assets for a direct strategic/policy purpose.
- Enhance the value and marketability of property assets enabling capital receipts to be used to support improved service delivery.
- Manage investment risk by investing in diverse sectors.
- Support the Council in maximizing the benefit from its financial assets in a risk aware way (not including standard treasury management activity)

The implementation of this strategy coupled with robust performance monitoring measures will ensure that the portfolio operates effectively and delivers value for money.

The Programme's strategy continues to be reviewed annually, and an updated strategy will be incorporated within the Medium-Term Financial Strategy which will be considered by Cabinet and full Council later in the year.

Rural Estate Management Review

- **Rent reviews 2024** – 14 notices were served for autumn 2024, with one exception which is linked to a lease renewal, these have all been agreed achieving a rental uplift of £60k (29%)
- **Rent reviews 2025** – 39 notices were served for spring 2025 of which 35 have now been agreed, achieving £73k rental uplift (17%). The remaining four remain with the Council's agents to be concluded.
- **Ongoing reviews** – internal review of the rental levels, tenancy agreements, etc. concluded that there is no scope for further notices to be served for autumn 2025, or spring 2026. Where rent changes are anticipated, these are linked to tenancy renewals.
- **Lease renewals September 2024** – all leases have now been agreed with a rental uplift of £15k, which equates to 30% increase achieved.
- **Health & Safety and Compliance** – a concerted investment of time and management has been made by the Rural management team, to complete a full audit of the Council's records. The team are developing a plan of action, which will ensure the Council is up to date with its statutory compliance obligations. It will involve a programme of works to ensure that all aspects of statutory compliance are at a satisfactory level within 2 years, projected to cost c.£860,000 funded from a combination of revenue budgets and sinking funds held by the IILP for such purposes. Alongside this, further work is progressing with the Corporate Health & Safety team to identify any additional requirements beyond statutory compliance matters.
- **Outstanding rent** – working with colleagues in EMSS and Legal Services, the levels of arrears has decreased by over £130k (vs the 2023 baseline) and a clear management policy is now in place to ensure that consistent action is taken, and issues are identified and addressed early. Legal action has been initiated against a number of debtors, with bankruptcy and possession proceedings being required in the most serious cases. It is anticipated that 2025/26 will bring substantial reductions in the legacy debt as legal actions take effect.
- **Documentation** – work is ongoing to address the issues of missing or incomplete documentation with a further 36 new tenancy agreements and 6 updated licence agreements have been issued. On completion of these, all live agreements will have appropriate documentation in place.

- **Inspections** – the annual inspections process is now embedded in normal management, with a particular focus on repairs and maintenance in the current year.
- **Repairs & maintenance** – following on from the annual inspections, work is now commencing to build up a comprehensive planned maintenance programme.
- **End of tenancy compensation** – along with reminders to tenants of the statutory protocols for tenancy compensation, work has been ongoing to collate and formalise agreements for improvements already in place to ensure accurate records are held.

Rural Estate Strategy

The overarching strategy for the Rural Estate for the period from 2025 to 2040 is currently being developed and will be subject to consultation with both internal and external stakeholders, including elected Members, over the coming months.

The Strategy will align with both the Council's Strategic Plan and IILP programme and confirm how Leicestershire's estate operates within a framework of national legislation, policies and agricultural markets, all of which should shape and influence how the estate is managed. The strategy will set out the vision, ambitions, challenges and opportunities for the estate for the next 15 years and will detail a comprehensive restructuring and investment programme in order that the estate can be resilient to future economic and structural changes within the industry whilst continuing to deliver positive financial benefits to the County Council. In addition, the strategy will detail how the estate will be managed in order to ensure that its implementation is both efficient and effective, and achieves value for money.



GLOSSARY

90 Day Debt: For LCC KPI purposes, debt over 90 days past due is performance benchmarked.

All Property Yield: All Property Yield is the calculation of the Yield (defined below) across all property asset classes (i.e., a portfolio yield)

Bad Debt: Bad debt is taken as any debtor account (most likely rent) which has remained due beyond 6 months. A bad debt provision is held against the debtor sum, and when the debt is cleared the provision is credited back to the revenue account.

Capital Growth: Capital Growth is the increase of the capital value, net of capital expenditure or income expressed as a percentage of capital employed. $(\text{Closing Value} - \text{Opening Value} - \text{Capital Expenditure} + \text{Capital Receipts}) / (\text{Opening Value} + \text{Capital Expenditure})$

Diversifiers: This describes investments which are not directly owned properties within the Leicestershire boundaries. As a result they are not subject to the same risks as directly owned property. The investments are made subject to the investment strategy for the liLP which was last updated in early 2024. The current investments include UK diversified commercial property and are accessed by investments in institutional property funds, global private credit funds which provide finance to corporate borrowers for a fixed term and global infrastructure funds where the underlying holdings include ports, toll roads and renewable energy assets.

Lease Expiry: Most commercial and agricultural leases do not automatically terminate on expiry but continue to “hold over” with the tenant bound to perform the obligations of the lease. There is no specific requirement to renew the lease, but the tenant usually gains a more flexible position in respect of notice to quit provisions. The Landlord remains bound by statutory restrictions on termination such as grounds for notice or time limitations.

Net Income Return: Net Income Return is the net income receivable expressed as a percentage of capital employed. This differs from the Initial Yield as it considers costs of ownership, including capital expenditure. $(\text{Net Income}) / (\text{Opening Value} + \text{Capital Expenditure})$.

Rent Review: Commercial and agricultural leases usually allow for periodic review of rents. Most commonly on a 3 year cycle, the rent due is reviewed by negotiation and reference to comparable rents or a statutory formula. Occasionally rents will be reviewed by reference to RPI or other inflationary measures, although these are less common for the types of assets held by liLP.

Rent Roll: The rent roll is the total annual income achievable by the property without deduction for rental allowances (i.e., rent-free periods) or other incentives, back-dated charges, premiums, or non-rental charges.

Sinking Fund: A sinking fund is an accounting device whereby funds are held on the balance sheet to offset or mitigate possible future costs incurred such as major incidents, significant revenue expenditure, etc.

Total Return: Total Return is the sum of the Capital Growth and Net Income Return.

Voids: Where commercial or agricultural property is vacant but physically capable of being leased or occupied it is classified as a void; property which does not meet statutory requirements for letting and is pending refurbishment, or unoccupied but leased is not included within the void figures.

Yield: Yield is the rental income expressed as a percentage of capital value. $(\text{Rental Income}) / (\text{Opening Value})$. In the context of this report, yield is used as a valuation comparator rather than solely as an expression of returns.



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