



NORTH HERTFORDSHIRE DISTRICT COUNCIL

Property Acquisition & Development Strategy

2020/21 - 2025/26



Introduction

North Hertfordshire District Council's (NHDC) Commercial Strategy outlines the ongoing financial challenges facing the public sector. This Property Acquisition & Development Strategy builds on the Commercial Strategy by setting out NHDC's core goal and objectives for pursuing property acquisitions and developments during the next 5 years. The Strategy's core goal is to secure property opportunities for the purposes of NHDC's functions or property opportunities that provide benefits, improvement or development of NHDC's area. The goal is expressed through a set of objectives in the Strategy. This is part of a continued drive to improve the economic resilience, environmental well-being and social fabric of NHDC's communities.

Property acquisition and development offers a range of advantages to NHDC and its community. As well as the ability to underpin NHDC's functions or the vitality of its district, property generally offers stable returns over the longer-term as it is insulated to an extent from market volatility. Returns are relatively stable since they come from both rental income and capital value appreciation. The latter is realised upon disposal of property and can be used to fund new capital expenditure. Property acquisition and development, though, also poses risks. For example, greater illiquidity makes it harder to access the capital outlay made. Acquiring and developing property requires careful planning and rigorous evaluation to achieve the goal and objectives of the Strategy whilst mitigating risk.

This Property Acquisition & Development Strategy establishes a robust framework for the identification and safe delivery of suitable property acquisition and development opportunities, in pursuit of the Strategy's core goal. It sets out a rigorous governance and appraisal process for NHDC to safeguard the capital expenditure on those opportunities. The Strategy is designed to protect the value of taxpayers' resources.

This Strategy focuses on protecting the long-term security of capital outlay by NHDC, whilst minimising risk to NHDC's capital. The Strategy also aims to help secure positive financial returns wherever possible. The Strategy has regard to the economic, environmental, social and community value of property acquisition and development decisions, for example those that afford NHDC opportunity to influence the amenity and environment of settlements in the district.

The Strategy is structured in a way that enables NHDC to pursue suitable acquisitions and development with the agility and efficacy required in the competitive marketplace. Competition for prime assets is strong, driven by low gilt yields, low borrowing rates and limited new supply.

Finally, this Strategy is aligned with the context of NHDC's Investment Strategy.

Scope of Strategy

The Property Acquisition & Development Strategy focuses on:

- *Direct* acquisitions of property, both buildings and land. *Indirect* acquisitions - be it through property investment funds or property companies - are outside the scope of the Strategy.
- Acquisition of *existing tenanted* properties.
- Acquisition of *value add* opportunities, i.e. properties where additional revenue and/or capital value can be generated from existing properties by:
 - Improved asset management.
 - Repurposing by change of use and conversion.
 - Refurbishment and capital enhancements.
 - Pursuing development potential.
 - Lease regearing*.
- Pursuing value add opportunities for properties already owned by NHDC.
- Acquisitions by *agreement* rather than using compulsory purchase powers.
- NHDC in its capacity as a local authority, not as a trading company.

Statutory powers

The Strategy acknowledges the following important factors:

- The need to identify the relevant statutory powers afforded to NHDC in its capacity of *local authority*, chiefly under the Local Government Act 1972.
- The current restrictions placed on NHDC in pursuing the opportunities of the Localism Act 2011 due to NHDC not having a trading company subsidiary at present.

Appendix 4 outlines the main Acts of Parliament and provisions this Strategy acknowledges.

Conflicts of interest

There is a possibility that those involved in implementing the Strategy may have actual or perceived conflicts of interest, be they Council Members, directors, officers or external advisers. From the outset, all those involved shall familiarise themselves with, and abide by, NHDC's Managing Organisational Conflicts in Council Roles & Duties, NHDC's Code of Conduct for Members and NHDC's Employee Conflicts of Interest Policy as appropriate.

Structure of Strategy

The Strategy addresses eight key aspects of property acquisition and development, as follows:

(1) Property acquisition & development objectives	<i>Page 5</i>
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(3) Identifying acquisition & development opportunities	<i>Page 6</i>
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(1) Property acquisition & development objectives

NHDC’s primary objectives for property acquisition and development are shown in Table 1:

Primary objectives	Practical examples
<p><i>To identify and pursue property acquisitions and developments that.....</i></p> <p>(1) Underpin or enable any of NHDC’s functions and corporate objectives <i>or</i> Benefit, improve or develop NHDC’s area.</p> <p>(2) Adhere to the principles of the prudent management of NHDC’s financial affairs.</p> <p>(3) Generate a net minimum return of 1.5% per annum above financing costs (interest and Minimum Revenue Provision).</p> <p>(4) Contribute to generation of extra revenue.</p>	<p><i>Acquisitions and developments that achieve and promote the following outcomes will signify achievement of the primary objectives:</i></p> <ul style="list-style-type: none"> • Supporting economic resilience, environmental sustainability or social fabric of NHDC’s town centres (perhaps within a regeneration programme, although noting that substantial redevelopment is likely to be outside the funding allocated). • Supporting enterprise, business rates retention, employment growth, place-making and public well-being in NHDC’s area. • Refurbishment or conversion of buildings to enhance rental income, environmental credentials and mitigate holding costs. • Reducing NHDC’s revenue costs by acquiring freeholds of rented operational property. • Acquisition of property that provides complementary benefits or value synergies for NHDC’s existing property portfolio. • Acquisition of property providing secure, long-term income to match NHDC’s long-term spending requirements, financial objectives and corporate strategy.

Table 1: NHDC’s property acquisition & development objectives

If a property opportunity demonstrates capacity to deliver NHDC’s primary objectives, the opportunity will be accepted for further consideration. If not, the opportunity will be rejected.

(2) Acquisition & development benchmarks

Appraising opportunities prior to acquisition and development, and monitoring their performance post-acquisition, will be conducted against a set of agreed criteria, benchmarks and performance indicators.

Sources of data that will aid this process include:

- Local property agents.
- National property companies.
- Royal Institution of Chartered Surveyors.
- Research by academic institutions.
- Investment Property Databank (IPD).

Because no two properties are identical, data from all sources must be diligently analysed when relating it to a particular property or market. Further, data must not automatically be taken at face value. NHDC will use its property market knowledge and experience and, where necessary, the advice of external independent experts, to sense-check data to ensure accurate appraisals and effective monitoring of acquisitions and developments.

(3) Identifying acquisition & development opportunities

Research

NHDC will look to widen its inclusion on the property mailing lists of local and national property agents and auctioneers. NHDC will build its relationships with the property agency fraternity to increase awareness of potential opportunities.

NHDC will also need to allocate personnel to frequently contact agents and auctioneers and to scour property media and research so opportunities can be assessed in good time. This will assist in formulating realistic, robust and competitive bids for suitable acquisition or development opportunities.

(4) Acquisition & development funding

Funding sources

Aside from grant funding that may be obtained, NHDC's Investment Strategy will decide how acquisitions and developments are funded.

Specific sources of funding might include:

- Central government, for example Homes England*.
- Hertfordshire Local Enterprise Partnership (LEP).
- Local Government Association (LGA) for grant funding independent expertise.
- Collaborative (joint) ventures with other public sector bodies, perhaps through the One Public Estate initiative.
- Joint ventures with housing associations or private sector organisations to share the risk of borrowing (particularly where synergistic value can be tapped).

NHDC can borrow to acquire and develop property for the purposes of NHDC's functions or for the benefit, improvement or development of its area. In its capacity of local authority, NHDC cannot borrow to acquire or develop property only for the purposes of achieving net income. However, this does not necessarily preclude NHDC generating a surplus from property acquired or developed pursuant to the Strategy.

NHDC shall have regard to CIPFA's* Prudential Code* in funding property acquisitions and developments, demonstrating value for money in borrowing and ensuring the security of such funds. To ensure prudent management of its financial affairs, NHDC shall ensure any borrowing costs can be serviced from the additional income generated from assets acquired.

(5) Location of acquisitions & developments

Location scope

As a local authority, section 120 of the Local Government Act 1972 permits NHDC to acquire property by agreement, both inside and outside its area, where the purposes of that acquisition is for:

- any of its functions under this or any other enactment, or
- the benefit, improvement or development of its area.

Further, section 120 permits NHDC, as a local authority, to enter agreements with other local authorities to acquire property on behalf of both or all of them in accordance with arrangements made between them. Those authorities can also make arrangements as to the subsequent occupation and use of the land.

Few opportunities are envisaged to arise *outside* NHDC's area that will underpin or enable its functions and benefit its area. Such opportunities are likely to be limited to those immediately adjacent to NHDC's area. Examples include sites that can be assembled with land already owned by NHDC to promote a viable development or marriage value, for the benefit of NHDC's area.

Suitable property opportunities that do arise outside NHDC's area must be assessed prior to acquisition or development for their advantages and disadvantages. Advantages may include:

- Diversification of risk by acquiring in more than one location.
- Reduced concentration in a single market lessening the chance of NHDC establishing a buyer monopoly market failure.

Disadvantages may include:

- NHDC crowding out another local authority's ability to acquire in its own area.

To help address this disadvantage, collaboration or an alliance agreement between NHDC and other local authorities is encouraged by this Strategy, in accordance with Section 120 of the Local Government Act 1972.

Sequential approach

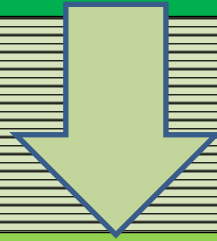
Where NHDC has a choice of location in which to acquire or develop property, NHDC will prioritise its district. Table 2 on the next page explains this approach further.

A:

NHDC's district

*Property acquisitions and developments in NHDC's district prioritised over other locations.
Reasons include:*

- Helps stimulate and support the viability and vitality of local areas.
 - Supports a local economic multiplier effect.
 - Supports business rates retention for NHDC's district.
 - Helps reduce property management costs.
- Familiarity with local property market strengthens acquisition and development decisions.



B:

Outside NHDC's district

Property acquisitions and developments outside NHDC's district will be considered when:

- Opportunities arise for land assembly with NHDC's existing portfolio to enhance function/value/income.
- Opportunities arise for joint acquisitions, ventures or partnerships with bodies whose functions or strategic objectives align with those of NHDC, to spread acquisition costs/risk and promote economies of scale. For example:
 - Hertfordshire Property Partnership members.
 - One Public Estate members.
- Opportunities arise to invest in properties that directly/indirectly benefit NHDC's district.

Table 2: Priority of location

(6) Risk management & governance

Background

As a local authority, NHDC is required to be prudent with its financial resources and funds. Prudence is attained by upholding its treasury management principles. Statutory guidance issued by the Ministry of Housing, Communities & Local Government (MHCLG) has broadened the scope of treasury management principles. NHDC is required to assess the security, liquidity and yield of its capital assets that it holds for purposes other than service delivery.

- (A) **Security:** how safe is the underlying capital deployed in an asset. This depends on the susceptibility of assets to value and market condition movements.
- (B) **Liquidity:** how easy is it to access the capital. This depends on time to sale, probability of sale and the costs associated with transacting.
- (C) **Yield:** the income return on an asset, such as the rental income or interest received from holding a particular asset.

The statutory guidance also now requires a consideration of the full costs of holding assets, including both revenue and capital maintenance. It encourages taking a longer term view of this expenditure, i.e. 10 years and beyond.

Four fundamentals of property assets

To reinforce these principles and guidance, NHDC will appraise the quality of all property acquisition and development opportunities against the following four fundamentals.

- ✓ 1. Security of capital.
- ✓ 2. Security of income: *in real and nominal terms*.
- ✓ 3. Liquidity: *ease and cost of disposal*.
- ✓ 4. Ease of management: *ease and cost of managing and holding assets*.

The yield or rate of return of a property acquisition or development reflects the four qualities listed above. Yield is primarily a function of both capital value and rent. Lower yields generally indicate that an asset attracts a lower degree of risk due to factors which include security and regularity of income. Yield will vary according to the market and nature of asset, including its location, tenant covenant and lease terms.

No property acquisition or development will simultaneously satisfy all four fundamentals; each can be mutually exclusive. NHDC officers and decision-makers will therefore need clarity as to which criterion is most important to NHDC when considering each property opportunity. This decision is influenced by NHDC's objectives outlined earlier in Table 1.

Risk expectations

Notwithstanding risk management and governance, NHDC must be aware that directly acquiring or developing property will always incur risk. Risk takes many forms, such as:

- Property is relatively illiquid compared to alternative assets. It can take a long time to sell and realise the capital invested.
- Turbulent property markets and volatile economic conditions can cause capital value depreciation and failure to recoup initial outlay.
- Costs of acquisition, disposal and management. Most if not all costs, such as transaction costs, are unlikely to be recovered if an acquisition or disposal is aborted.
- Rental income streams may be reduced or interrupted, for example during tenant voids or upon tenants defaulting on their rent payment obligations in their leases.
- Void periods may incur direct costs to NHDC including business rates, facilities management, repairs and maintenance, insurance and utilities. Such costs may not be balanced by income during void periods.
- Inflationary spikes eroding rental income and returns in real terms.
- Building obsolescence and physical deterioration may incur unexpected capital expenditure for NHDC. Examples of events that may lead to these are changes in technology and occupier demands, tenants' failure to honour lease repair obligations, and/or new legislation such as regarding energy efficiency.
- Change in law or guidance may further limit NHDC's ability to borrow for the purposes of the Strategy.
- Changes to taxation of property.

Risk parameters

NHDC should appraise property acquisition and development opportunities yielding a net minimum return of above 12% with extra vigilance as such high yields indicate a high risk opportunity. NHDC should choose to prioritise security of capital and liquidity over yield/return.

NHDC should carefully consider and question the rationale of property opportunities that yield below a net minimum return of 1.5%. The return received should reflect the risks involved and the management required.

Illiquidity is an inherent risk in property acquisitions. Measures that NHDC should take to mitigate this and other risk include:

- Acquire across a range of property sectors. This provides opportunity for NHDC to effect sales in the more liquid sectors should this be necessary.
- Assemble a diversified property portfolio in terms of lot size. This enables NHDC to access a breadth of purchaser types, for example small local investors, listed property companies or institutions.
- Acquire modern properties which are designed by building information modelling (BIM) and fully integrated with technology, for example sensors that measure a building's environmental performance. These will help present a property's full service history more transparently, which is expected to support liquidity.
- Avoid high yield high risk properties, as these are likely to signify significant illiquidity, for example leaseholds with fewer than 80 years unexpired.
- Avoid specialist properties, for example those only suitable for a narrow segment of the occupier market and lacking flexibility to adapt to a wider market without significant capital expenditure.
- Avoid acquiring properties subject to onerous conditions or charges, for example overages or restrictive covenants.
- Make use of specialist external advice.

Risk to NHDC will be assessed both on an individual asset basis and on a cumulative basis which considers the interaction of asset risks on the portfolio.

Contingency funds

By acquiring property, periods will inevitably be encountered when certain properties' rental income is outweighed by their outgoings. Such periods can be expected (for example known lease end date) or unexpected (for example tenant default). Where NHDC receives exceptionally high yields in the early years of an acquisition or development that reflects the risk of a future event then it will consider pooling some of those excess returns into a specific reserve.

NHDC will also consider the risk of reduced income and void holding costs when setting its minimum General Fund balance.

Property Scrutiny Group (PSG)

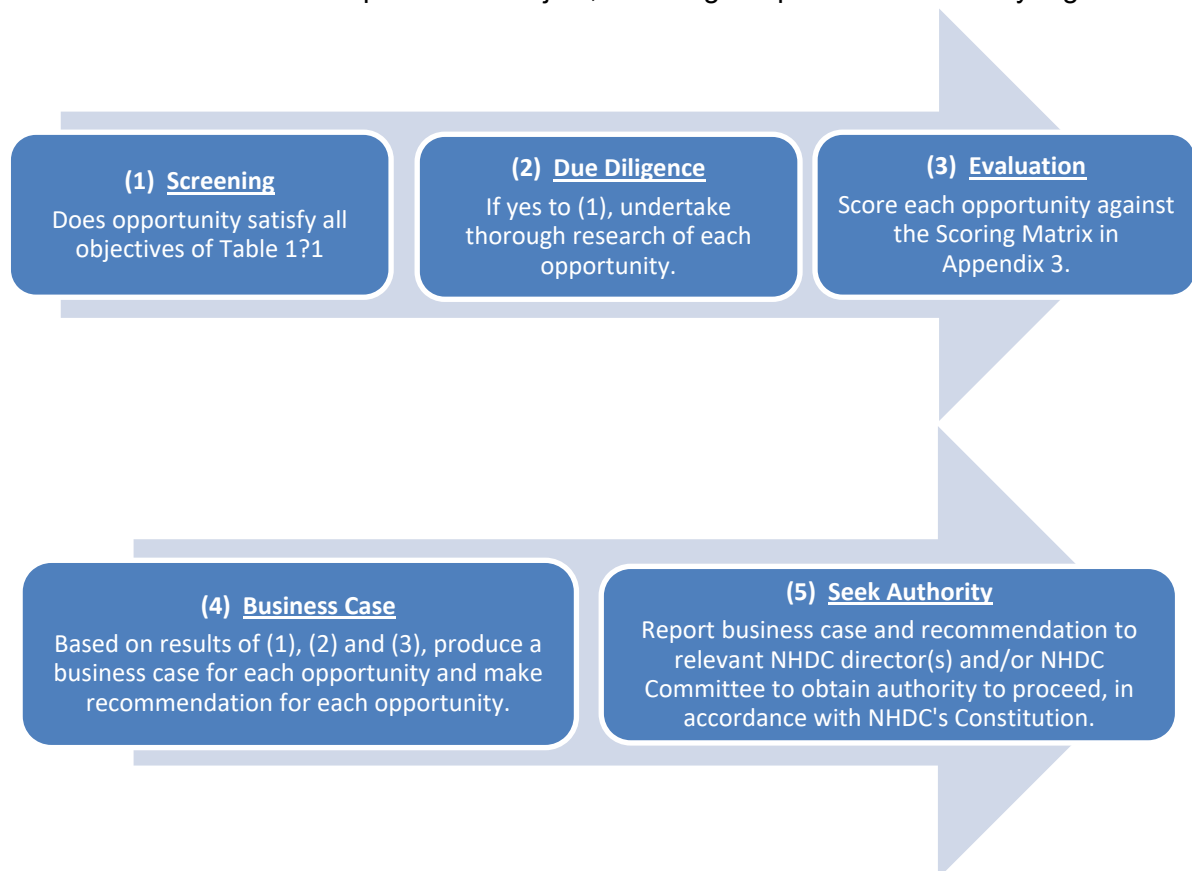
NHDC's PSG will appraise, and make recommendations on, property acquisition and development opportunities. The PSG will base appraisals and recommendations on this Strategy. The PSG will operate within the Terms of Reference of Appendix 1.

The PSG will comprise the following core group of directors and officers from NHDC:

- Service Director: Commercial (*Chair of PSG*).
- Service Director: Resources (*Deputy Chair of PSG*).
- Senior Estates Surveyor.
- Commercial Manager.
- Accountancy Manager.
- Contracts & Property Solicitor.

The group will benefit from skills and experience of professionals across the property, commercial, financial and legal spectrum. External advisers with relevant qualifications, skills and experience will be commissioned as required. In time, specific independent advice may be sought on how and which property acquisitions and developments can be pursued and structured to best advantage upon setting up of a Property Company.

The PSG will consider each property acquisition or development opportunity and make recommendations on which to pursue and reject, following the process outlined by Figure 1.



¹ All objectives in Table 1 are deemed mandatory by this Strategy.

Figure 1: PSG process & actions

The Service Director: Commercial reserves the right to consult on recommendations of the PSG with other NHDC directors, the Executive Member for Enterprise and Co-operative Development and the Executive Member for Finance and IT.

All recommendations of the PSG to acquire a property or pursue a development will then be reported to the relevant NHDC director(s) and/or NHDC Committee to obtain authority to proceed, in accordance with NHDC's Constitution. If commercially sensitive or personal information must be conveyed to NHDC directors and Committees to enable full consideration of a property opportunity, this must be reported under Part 2 conditions.

This process will be kept under review to ensure it provides the required level of governance for NHDC whilst also allowing sufficient agility to secure suitable opportunities in the competitive property market.

(7) Due diligence*

Property portfolio

NHDC is aiming to build up a property portfolio that reinforces the four fundamentals of property assets discussed earlier – security of capital, security of income, liquidity and ease of management. For risk control purposes, a proportional portfolio should be aimed for. This is one in which overall capital value and rental income is reasonably balanced across a range of property sectors incorporating a range of attributes.

To help ensure proportionality, diversity and minimum risk when building a property portfolio, regard should be made to NHDC's overall investment portfolio, i.e. including non-property assets.

This will help achieve a prudent risk balance between the four fundamentals, and help secure the core goal and objectives of NHDC that are set out in this Strategy. A proportional and diversified portfolio will help insulate NHDC against turbulence in one specific asset type or sector to avoid this disproportionately impacting on NHDC.

In terms of property sectors, acquisitions or developments across the following sectors will ensure a diversified portfolio:

- Light industrial, including:
 - Warehouse & distribution.
- Offices.
- Retail, including:
 - Trade counters.

- Residential, including:
 - Private homes.
 - Affordable homes.
 - Non-cyclical markets, e.g. senior living and student accommodation.

- Alternatives, for example leisure.

Traditionally, the industrial, office and retail sectors have featured significantly in the portfolios of property purchasers and investors, with a fairly even split between all three sectors.

However, this traditional mix is not recommended by this Strategy. In particular, with retail undergoing structural shifts in demand because of competition from e-commerce and changing consumer shopping habits, allocating a high proportion of overall capital outlay to retail would, it is considered, expose NHDC to excessive risk.

Retail acquisitions should be restricted to retail offering consumer convenience and good customer “experience”, hybrid retail schemes* and retail affording value add opportunities, combined with regenerative benefits. Retail as part of a mixed development with other uses is possible too.

Good quality, accessible industrial/warehouse units with good tenant covenants are benefiting from a sustained demand in and around NHDC’s district. Demand from a better quality tenant base for small to mid-sized industrial, warehouse and delivery hub units is increasing. The shift to online commerce, demand from omni-channel tenants, need for storage and requirement for last-mile logistics space is driving demand. This combined with the limited supply of such units make acquisitions in this sector a reasonable proposition. NHDC should be aware competition for these units from investors is keen as they are increasingly viewing the defensive nature of this asset class as a hedge against economic uncertainty. Further, assets serving the logistics market are not without their own structural challenges such as the rise of autonomous trucks and stock procedures. To accommodate such technological advancements, NHDC may be compelled to spend capital on such assets to maintain their tenant appeal and delay onset of obsolescence.

Regarding residential, it is reasonable to envisage the sustained and growing demand for residential units in and around NHDC’s district coupled with supply imbalance make this a sound acquisition or development proposition for NHDC. Residential schemes can make suitable long-term acquisitions by offering relatively secure, stable, long-term often inflation-linked income streams, with limited void risk. However, the high capital prices of residential assets in NHDC’s area, together with their relatively onerous management needs, significantly suppress available yields. The higher yields are more often associated with residential property schemes offering value add opportunities, for example development or conversion of under-utilised properties, or those with scope to improve asset management.

In general, assets with potential for long-term income or capital value enhancement via asset management, lease regearing or renewals and/or through development will be considered.

Cautionary note on residential property

Despite the benefits of residential property, this Strategy recommends NHDC acquires or develops residential property with extra caution, particularly if it aims to hold and let out that property. As a local authority, letting out residential property can place NHDC at risk of tenants gaining Right to Buy power over the property. If exercised, such power may require NHDC to dispose property at significant discount* to market value. In addition, NHDC can be placed at risk from residential tenants acquiring freeholds from NHDC under enfranchisement legislation. Further, recent government plans to abolish section 21 notices* of the Housing Act 1988 and “no-fault” evictions should also be noted. These plans, if enacted, are positive for residential tenants by increasing their security of tenure. However, they may leave landlords with less management flexibility and place greater onus on ensuring future tenants provide good covenant. Ultimately though, despite the government plans, landlords will still have the liquidity of their asset protected through the right to recover possession on sale.

Apportionment between property sectors

This Strategy does not recommend a static target apportionment of expenditure across the different property sectors. This is because:

- Property opportunities, particularly higher yielding ones such as value add schemes, will not present themselves to the market at regular or fixed intervals. Some years may see many opportunities, others fewer. NHDC needs to be ready to appraise and pursue suitable property acquisitions or developments as and when they arise.
- Where mixed use opportunities arise, the exact proportion of expenditure between the uses will be different for each scheme, influenced by myriad factors such as specific site conditions, planning conditions and scheme viability.
- Market changes and economic volatility, or changes in NHDC’s objectives, can lead to a static target apportionment becoming unfit for purpose. For example, to support the portfolio’s resilience in volatile economic conditions, NHDC should give greater priority and weight to counter-cyclical property sectors*, such as alternative sectors, or to “mission-critical”* properties.
- A static target apportionment may, with the passage of time, fail to satisfy or encapsulate all of the security, liquidity and yield governance requirements.
- NHDC’s overall investment portfolio, i.e. including non-property assets, may change over time. Recommending a static proportion of expenditure in certain property sectors may lead to disproportional concentration in one sector, exposing NHDC to unmanageable risk levels.

Instead, Figure 2 provides an indicative chart illustrating the risk-return trade off for the various property sectors in NHDC’s district at present. The proportion of capital outlay that NHDC decides to place into each property sector, or the priority or weight it assigns to any one sector, cannot be prescribed or reliably predicted by this Strategy. This is a decision that NHDC must take each time it assesses potential acquisition or development opportunities, based on assessing each sector’s risk-return profile at the time, in pursuit of the Strategy’s objectives.

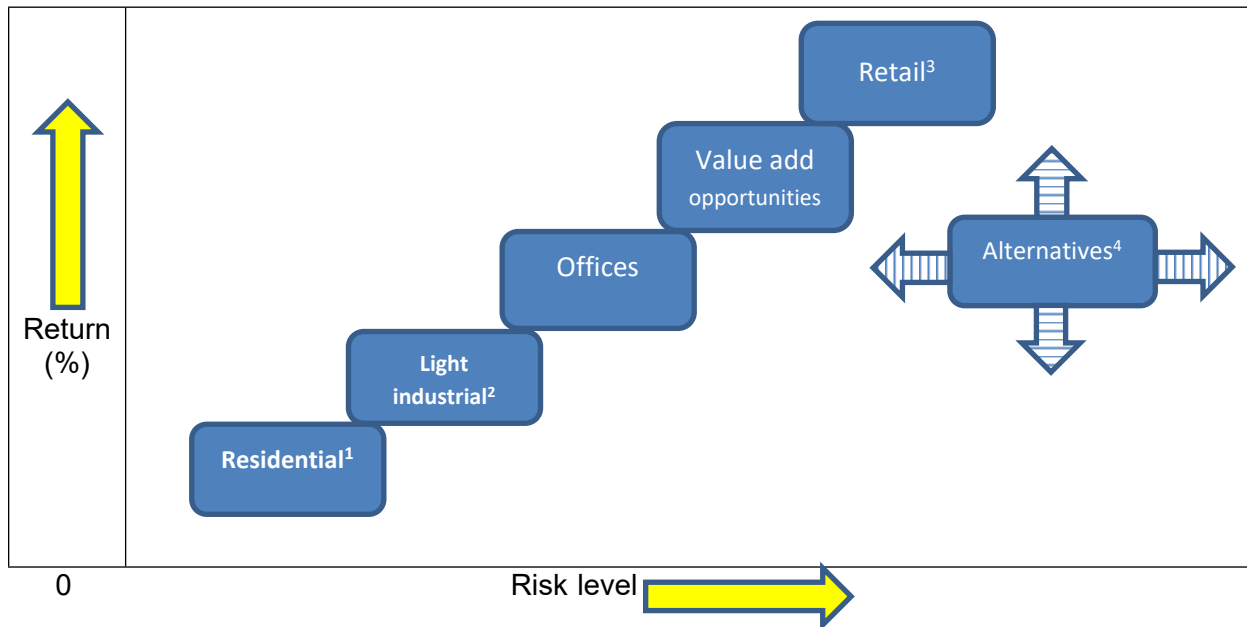


Figure 2: Risk-Return profile of property sectors

- 1 Primarily refers to private homes, not affordable homes or non-cyclical markets. Disregards Right to Buy risk.
- 2 Includes warehouse and distribution property.
- 3 Primarily refers to market town centre-dominant and secondary shopping centres, not trade counters or other retail.
- 4 Alternatives is a wide category to define, and one often comprising novel property concepts and markets. The risk-return profile of the Alternatives sector is therefore particularly uncertain.

Review of property portfolio

NHDC must frequently review the composition of its property portfolio to ensure it remains proportional and diversified between sectors. The composition should be viewed in the context of NHDC’s:

- Existing property portfolio; and
- Investment Strategy.

The purpose is to assess the overall risk-return profile to which NHDC is exposed, in pursuit of the Strategy’s objectives. NHDC’s existing property portfolio mainly comprises industrial/commercial ground rent investments. These are one of the safest forms of property investment. This allows NHDC a degree of safety margin in acquiring property by providing a stable foundation and balance for an expanding property portfolio.

NHDC should monitor the performance and proportionality of the property portfolio over time and, if necessary, rebalance it in light of market demand and supply movements and their

effect on risk-return. Such movements can be influenced or triggered by a range of factors and stakeholders, including investors, owner-occupiers, tenants, lenders and local/national government. Adjustment of the portfolio will mainly be by property disposals, new acquisitions and lease regearing. Property disposals will be facilitated if the assets have greater liquidity.

Selection criteria

Each property acquisition and development opportunity will be appraised by NHDC against the key qualitative and quantitative asset criteria detailed in Appendix 2, Tables 1 – 9. The criteria are summarised below:

- Location.
- Tenant Covenant.
- Building Performance.
- Lease: Repairing Obligation.
- Lease: Rent Review Mechanism.
- Lease: Length of Occupational Lease.
- Tenure.
- Lot Size.
- Net Minimum Return.

Scoring Matrix

The Scoring Matrix in Appendix 3 enables the relative merits of a property acquisition and development opportunity to be evaluated against the criteria detailed in Appendix 2. The overall score for each opportunity can then be viewed against NHDC's objectives of this Strategy, its benchmarks or alternative opportunities.

Whilst property risk cannot be entirely eradicated, the Scoring Matrix helps to assemble a well balanced and diversified property portfolio across a range of criteria, including location and lot size. In turn, this will support an optimal trade off between risk and return and help NHDC secure the Strategy's objectives.

The Scoring Matrix in Appendix 3 summarises the key property criteria. The overall purpose of the Scoring Matrix is to assess how each opportunity is likely to perform against the four fundamentals of property assets discussed earlier. The four fundamentals are reiterated below, alongside their level of importance in the Matrix:

- ✓ 1. Security of capital
- ✓ 2. Security of income: *real and nominal terms*
- ✓ 3. Liquidity
- ✓ 4. Ease of management.

The asset criteria are assigned a Weighting in Appendix 3. The Weighting scale ranges from 1 (low Weighting) to 4 (high Weighting) and corresponds (inversely) to the level of importance assigned to the four fundamentals, as follows:

- | | |
|--|------------------------|
| 1. Security of capital = | WEIGHTING OF 4. |
| 2. Security of income: <i>real and nominal terms</i> = | WEIGHTING OF 3. |
| 3. Liquidity = | WEIGHTING OF 2. |
| 4. Ease of management = | WEIGHTING OF 1. |

Where an asset criterion addresses two or more of the fundamentals, it is assigned an additional Weighting according to the level of importance of those other fundamentals.

So, for example, the criterion of *Tenant Covenant* addresses the highest level fundamental of **Security of capital**, plus the second most important fundamental of **Security of income**, plus the third most important fundamental of **Liquidity**, and the fourth most fundamental of **Ease of management**. *Tenant Covenant* is therefore assigned a Weighting of 10 (4 for Security of capital + 3 for Security of income + 2 for Liquidity + 1 for Ease of management).

Further, the Scoring Matrix scores the quality or performance of a property opportunity against each asset criterion. A score of 5 is awarded for those that have “Excellent” quality or performance, down to 1 for “Marginal / Not Acceptable”.

The Weighting and the quality score are then multiplied together for each property opportunity. Those opportunities that meet the threshold score weighting of 207 will then progress to be subject to a business case by the PSG.

Property research

Due diligence of properties considered for acquisition or development will include the essential background research and enquiries to fully understand the legal, financial, commercial and constructional circumstances and prospects of each property.

Timeframe & frequency

This Property Acquisition & Development Strategy is aimed at the next 5-year period. The Strategy will be kept under annual review by the PSG during this period, paying particular attention to the following influential factors:

- Material changes in property market dynamics, particularly retail sector.
- Material changes in the economy, such as the Brexit outcome.
- Legislative developments, in particular property energy performance regulations.
- General permitted development rights in Town & Country Planning.
- Advancements in “proptech”, for example use of artificial intelligence to improve the efficiency of pre-acquisition due diligence.
- Changes in NHDC’s objectives.
- NHDC’s staffing resource requirements, to ensure continued effective operational and risk management of an expanding property portfolio.
- The setting up of a trading company subsidiary to NHDC. No such company currently exists but if one was established this may widen the scope of property opportunities that can be pursued.

Glossary

Terms in this Strategy highlighted by an asterisk (*) are defined or explained below.

CIPFA: Chartered Institute of Public Finance and Accountancy.

Counter-cyclical property sectors: Those less exposed to the changing fortunes of the economy.

Discount: Local authority Right to Buy sales averaged a 42% discount from selling price in 2017/18 in the UK, based on latest available data. Source: MHCLG.

Due diligence: An investigation or audit of a potential property acquisition or development to confirm all facts, including the review of financial records. Refers to the research carried out before entering into an agreement or a financial transaction with another party.

Homes England: Homes England is the non-departmental public body that funds new affordable housing in England. Founded on 1st January 2018 to replace Homes and Communities Agency (HCA).

Hybrid retail scheme: Retail property comprised of retailers operating in the bulky goods and food sectors.

Mission-critical properties: Properties whose availability, as a factor of production, is critical to the success of a business. Examples are a manufacturing plant that produces the goods that generate a significant element of the tenant's profits, or a research & development laboratory of a pharmaceutical firm.

Prudential Code: A framework produced by CIPFA supporting local strategic planning, local asset management planning and proper option appraisal. Objectives of the Prudential Code are to ensure capital investment plans of local authorities are affordable, prudent and sustainable.

Regearing (as in lease regearing): A lease regear replaces one lease with a new one, on renegotiated terms. The landlord and tenant are free to do this at any time which may be desirable when the parties' commercial objectives may have altered in recent years.

Section 21 notice: A section 21 notice under the Housing Act 1988 is a "no fault" notice. This means that a landlord of a residential property can ask a tenant to leave after the fixed term of the tenancy has ended without giving a reason.