



Bruntwood – Proposed new retail bond

Ticker: BRUNT

Issuer	ISIN	Coupon	Maturity	Comments	Issue amount	Min Piece	Increments	Price	YTM	Spread to convention
Bruntwood Investments Plc	XS0947705215	6%	24/07/2020	Existing deal, secured, 1.25 point exchange fee	£50m	£2k	£100	101.25	2.92%**	+240bps
Bruntwood Bond 2 Plc	TBC	6%	2025	Unsecured*	TBC	£2,000	£100	100	6%	+550bps

* Guaranteed by Bruntwood Limited & Bruntwood Management Services Limited – see group structure on page 2

** Settlement date 25th Feb 2020

Background

Bruntwood is an unlisted property company that owns and manages a portfolio of commercial property across Greater Manchester, Leeds, Liverpool and Birmingham. The business was established in 1976 by the current CEO’s father, Michael Oglesby.

In September of last year, the group’s property and investments were valued at circa £1.25bn; the largest area of investment is to Manchester’s City Centre – 41 buildings with an aggregated value of £756m; other exposures are as follows:-

Asset breakdown	Buildings	Value £m
Manchester City Centre	41	756.2
Leeds	5	109.9
Liverpool	6	107.1
Alderley Park (£1.2m sq ft Life Science & Tech Park)	144 customers	122.5
Greater Manchester region (Didsbury, Old Trafford & Warrington)	18	162.8
Birmingham	7	145.7

There are two operating divisions within the business - Bruntwood Works and Bruntwood Scitech. Works is predominantly a portfolio of office space. There are over 70 buildings across its office portfolio with accompanying facilities including gyms, cafes, business incubation and collaboration opportunities.

Bruntwood Scitech is a network of innovation districts that creates the environment (office and lab space, meetings rooms) and the ecosystem (business support services, scientific services, collaboration opportunities) for the science & tech sector. Since 2018 these assets have been held within a 50:50 joint venture with Legal & General, valued at £446m in September 2019. An abridged property snapshot is as follows:-

Property Snapshot	Total	Works	Sci-tech
Number of customers	2,606	1,958	534
Serviced desks	2,495	2,171	324
Valuation £m	1,468	991.1	441
Headline rent £m	102.7	74.6	22.8
Yield	7%	7.5%	5.2%

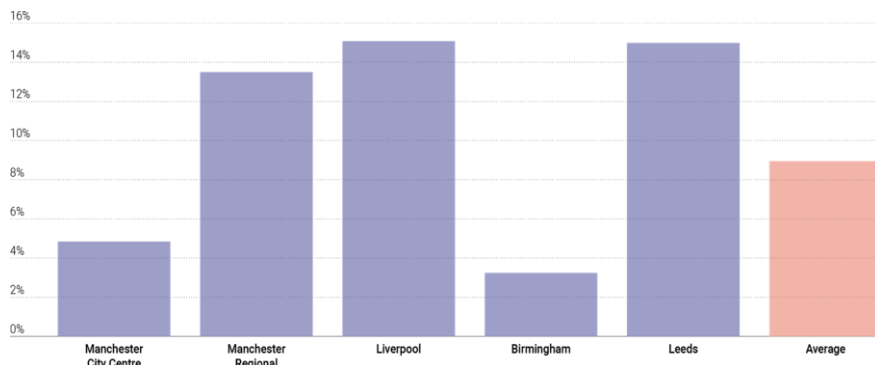
The group’s customer base includes large corporates, public sector, retail and SME – with this last type representing 44% of the overall portfolio. The group isn’t keen on single let occupancy due to the impact that that can have on property values towards the vacancy date. Instead the group target multi-let properties typically purchased at the end of first cycle when institutional owner doesn’t have the capability to deal with the vacant asset. More recently, there has been a move towards new build as part of a full product offering to meet customers’ expansion requirements. Concentration risk appears to be low with the top 10 customers by rent value representing around 10% of rental income with the highest paying customer – Network Rail – paying annual rents of c.£2m.

Bruntwood claims that 77% of customers are retained at the first break clause date, which is roughly in line with the industry average, however at maturity Bruntwood retains 66% which is some way ahead of the overall market at c.25%. Bruntwood likes

to cite high customer service for the outperformance - all sales and marketing is conducted in-house (whereas many owners outsource these functions). For this reason, Bruntwood asserts that it has a comprehensive knowledge of its customer base.

On vacancy rates the group states that it is currently within “churn” level, although it concedes unoccupied rates in regional Manchester and Liverpool (see below) have proved tricky to tackle since the 2009 financial crisis. Leeds is also high, but management commented that the figure is distorted by one large vacancy, which is now under offer.

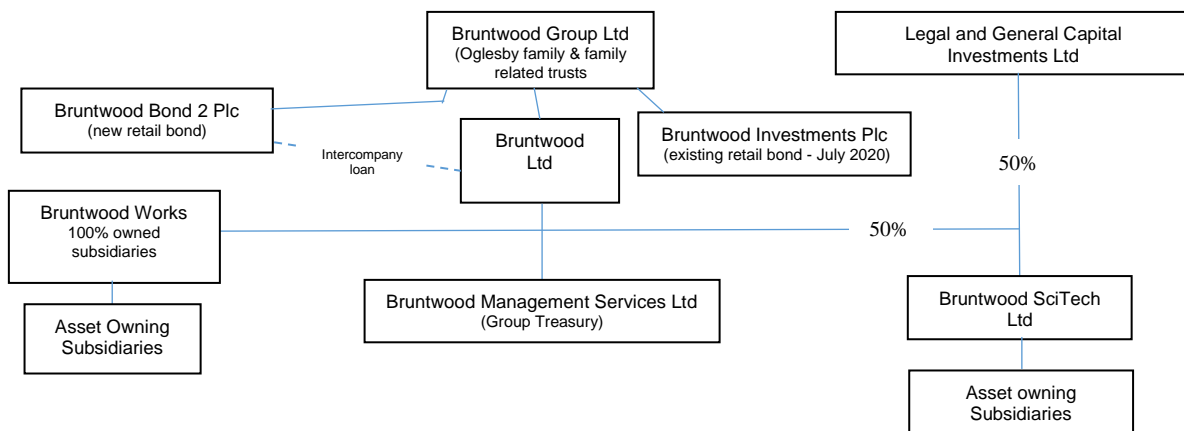
Vacancy rates:-



Average term to expiry of leases is currently 5.2 years with average to break of around 3.3 years. The market is increasingly demanding shorter more flexible leasing; this suits Bruntwood given that it has over thirty years’ experience in flexible products including short leases, coworking spaces and serviced offices

Ownership structure

The group’s topco is Bruntwood Group Limited, which is the family’s holding company. Intermediary holding company Bruntwood Ltd is where the group board sits; that company owns 100% of Bruntwood Works and 50% of Bruntwood SciTech (with the other 50% owned by JV partner Legal & General).



Proposed new retail bond (to replace the deal maturing July 2020)/

The group is proposing a new retail bond with a 5-year maturity which will be unsecured, although the deal will be guaranteed by Bruntwood Limited (board level holding company) and Bruntwood Management Services Limited which provides treasury functions to the group.

Key covenants are as follows:-

- Net debt to tangible fixed assets cannot exceed 0.75x.
- Parent guarantor must maintain £50m of net worth while the guarantor group must maintain £400m.
- Two semi-annual coupons must be maintained (tested twice per annum)
- No incurrence of additional financial indebtedness above 65% of tangible fixed assets.

A non-payment allows for 14 days for the group to remedy the default. A breach of other obligations, such as covenants above, allow thirty days of “breathing space”. Once these time limits have been exceeded the trustee, at its discretion, can issue an Acceleration Notice that states that the bonds are immediately due and repayable.

Abridged P&L (FRS102):-

Bruntwood Limited	Year to 30th Sept 2019	Year to 30th Sept 2018	Year to 30th Sept 2017
Revenue	£m	£m	£m
Rental income	93.4	87.6	82.1
Service charge	22.6	25.2	22.2
Property services	19.8	14	13.6
Development	24.3	6.5	6.5
Land disposal	-	0.94	7.1
Alderley Park disposal	-	3.4	-
Total revenue	160.1	137.7	131.5
Cost of sales	-98.8	-77.6	-73.5
Gross profit	61.3	60.1	57.8
Admin expenses	-23.6	-36	28
Operating profit	37.7	24.3	29.9
Share of results of JVs	3.78	0.226	-
Valuation gains	31.94	127.38	54.3
Derivative gains / losses	-3.3	5.99	6.6
Loss on revaluation of listed investments		-0.31	-1.2
Exceptional profit or loss	0.58	-12	2.5
Gain or loss on sale of investments	2.36	-0.11	6
Profit before interest & tax	73.1	145.2	98
Net interest payable	-21.3	-28.9	-26.1
Profit before tax	51.8	116.3	72
Dividends paid up to family holding company	1	14	-

Consolidated Balance sheet:-

Bruntwood Limited	At 30th Sept 2019	At 30th Sept 2018	At 30th Sept 2017
Intangible assets	0.08	0.19	0.15
Tangible	973.7	935.7	1,097.8
Investments in JV	112.1	104.3	-
Debtors within 1 year	102.8	64.5	74.5
Debtors more than one year	30.8	39.4	37.7
Development in progress	-	12.2	39
Current asset investments	-	-	1.3
Cash	17.1	14	16.4
Total assets	1,237	1,170	1266.9
Liabilities			
Debt in one year	-164.4	-133.81	-227.6
Debt over one year	-444.6	-459.6	-512.9
Provisions for liabilities	-17.96	-15.3	-23
Total liabilities	-627.0	-608.7	-763.5
Net assets	609.4	561.3	477.6

Guy Butler Limited

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Conclusion

Bruntwood has been in business for over 43 years, and despite a ~40% fall in values in 2008, the group has remained profitable under UK GAAP accounting. Since 2016 the group has however reported its figures under FRS102 which requires companies to report the movement in the valuation of assets as a component of profit before tax – management explained this would have led to a loss c. £80m in 2009 compared to the £12.m profit reported at the time. It also would have meant that the elevated profits between 2016 and 2018, which exceeded £70m per annum, would have been in the £10-£20m range, if reported under UK GAAP!

Bruntwood are long term players with a significant presence in their key regions, underpinned by a strong brand. That's reflected in the partnerships with both councils and universities intended to boost economic development and regeneration. We highlight the following strengths and weaknesses to an investment in the new 6% notes:-

Strengths:-

- > Shareholder's funds of £609.4m at Sept 2019
- > Average yield of wholly owned property portfolio of 7.3%.
- > Favourable technicals - limited new issuance in higher yielding GBP notes in recent months.
- > Average operating profits of £39m over past ten years - £37.7m in year to Sept 2019, which was 1.77x net interest payable.
- > Decent headroom versus the LTV component of its secured facilities (see Appendix 1) as well as passing rent to finance charge.
- > 70% of customers secured at lease break or expiry in year to September 2019.
- > We found management open and helpful regarding our enquiries.

Weaknesses:-

- > IFRS accounting means property revaluations will be carried through P&L which could lead to earnings volatility.
- > A measure of caution over ambitious growth plans which could see assets grow from £1.4bn to £2.7bn over five years. Commercial property can be particularly vulnerable in an economic downturn...
- > Vacancy rates on the high side in regional Manchester / Liverpool.
- > Unsecured notes which sit behind all the other charged facilities.
- > Private company which would be harder to recapitalise in the event of a breach of bank or bond covenants, although we would expect Chris Oglesby and his family to be supportive.

Please call the desk if you have any questions.

Rupert Harcus

Sources:- Roadshow presentation, draft prospectus, meeting with management, company accounts

Appendix 1

Debt position / asset values at Sept 19:-

Works Loans	Comment	Loan Size £m	Maturity	Sept 2019 Property values £m	LTV	Covenant limit
Existing Retail Bond		50	Jul-20	70	71.4%	100%
L&G		117	Dec-22	280.4	41.7%	65%
Syndicate (RBS/Santander/HSBC/Barclays)		198.9	Mar-22	390.8	50.1%	65%
Aviva		111.7	Dec-31	238.1	46.9%	80%
Didsbury	North West Evergreen development loan	3	May-20	6.2	47.8%	65%
K-Site	Development loans - Trafford Council	10.6	May-21	*	52.2%	100%
Headroom / Concession balances				-11.9		-
Total		491.2		973.6	50.5%	
Stretford Mall & Stamford	Development loans - Trafford Council	26.1	Oct-26	26.1	100%	-
K-Site	Development loans - Trafford Council	-		20.2		-
Cash / add back concession		17.1		11.9		-
Total - Works		500.1		1031.9	48.5%	
Sci-tech loans						
Syndicate (RBS/Santander/HSBC/ Lloyds)		110	Jul-22	408	27%	65%
Innovation Birmingham	Investment loan from Birmingham City Council	13	Apr-21	14.8	86%	100%
Citylabs 2.0	North West Evergreen development loan	3.7	Mar-21	17.4	21%	65% to cost
Uncharged		-		5.4		-
Total		644		1,478	45%	
Total (net 50% JV)		580		1,255	46%	

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