Government and Public Sector

31 October 2005

New Covent Garden Market Disposal

Disposal Options Review

PRICEWATERHOUSECOOPERS

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Executive Summary

The New Covent Garden Market ("Market") was moved to its current site in 1974. The issues surrounding both the organisation and the site stem from this move. The legislation put in place to protect the future of the Market is now viewed as a burden. The buildings reflect the needs of a market in the 1970's and the rate and pace of change in the fruit, vegetable and flower industries has been dramatic, meaning the Market has struggled to keep up with developments in these industries and over the past ten years the Market has stagnated.

An illustration of the complexity of the issues which are facing the Market can be found in the number of reports commissioned which have not resulted in any significant change to the market. The buildings are deteriorating, uncertainty prevails for the market traders and the Covent Garden Market Authority ("Authority") itself and yet the market sits on a potentially valuable site close to central London which is under-utilised.

There is a general wish from Defra to maintain the Market expressed by Ben Bradshaw as follows:

> *"We shall aim to secure arrangements which will maintain the Market as a going concern which can both accommodate the businesses which are established there and allow it to develop as a consolidated market as envisaged by the Saphir Report".*

However, there is no general agreement on what "the Market" means and this is of fundamental importance in ensuring a sustainable future. What is certain is that whatever "the Market" means now, it will have a different meaning in another thirty years. Enabling flexibility to respond to change within the food industry will be fundamental to the long term future of the Market. What is missing at this time is a strategic vision for how the Market will meet the challenge of responding to this change and how the Market should progress in the medium term both as regards its physical and economic shape.

Defra has responsibility for the Market through the Authority, the statutory organisation established through legislation to run the Market. The Authority owns the site at Nine Elms on which the Market is based. Defra wishes to disengage from the Authority and this report considers the options for doing this.

The key criterion for Defra is complete disengagement with no residual involvement in the Authority. Achieving this hybrid legislation will be necessary to allow the sale of the Nine Elms site and the transfer of the Market business to another organisation, and the dissolution of the Authority. It is our understanding that the earliest date for such legislation is 2007/8.

It is also important to Defra that the disengagement from the Authority happens as quickly as possible. This clearly needs to be balanced with the need for legislative change and the need to demonstrate optimum value for money on any disposal from Government.

This report considers two main areas; the Market business and the options for disposal of both the business and the Nine Elms site. On the basis of this analysis it recommends a route forward which is considered both deliverable and likely to achieve optimum value for money. Deliverability of any potential scheme is a key consideration and there is a wide range of stakeholders which could hamper progress, particularly if it threatens the long term future of the Market.

The Market is not operating on a long-term commercially viable basis. It currently generates a low return and is unable to fund the significant financial capital investment required to maintain the facilities at appropriate standards. Low returns also constrain the Authority's ability to redevelop the market. Further decline of the Market is inevitable unless capital is invested in its infrastructure.

As a result it is unlikely that the Market in its current form would be considered as either an attractive or commercially viable business proposition by a private sector investor. However, it is clear that the Market has valuable core assets such as its property base, established network of suppliers and clients, and its brand name/reputation which suggest that commercial value could be generated in the long term, subject to additional investment and business development.

Reform could be undertaken by the Authority with its new Chairman and Board currently acting as catalysts for change, although it is too early to comment on the substance and effect of their actions. Alternatively, the business could be reformed by a third party under a management contract.

Increasing both the rents and service charges towards commercial levels would help to create a sustainable business. However, such increases will inevitably impact upon the Market tenants and their ability to continue trading.

Reform would not, on its own, meet Defra's main objective of full disengagement by the earliest point at which hybrid legislation could be granted in 2007/8. Full turnaround of the business would have to wait until 2010 when the majority of lease agreements are due for renewal, although the procedures necessary for reform would have to be put in place much earlier. Reform would help maintain the market as a commercially and financially sustainable business which would help assure its long-term existence.

The disposal options analysed in this report take account of the need to reform the business. Disposal before the market had been reformed would put its future as a going concern in question. Implementation of any reform cannot be completed until 2010 when the majority of leases are to be renewed. However, a disposal before then could be made satisfactorily, provided that Defra was satisfied that a reform programme was in place and would be implemented.

Understanding the strategic vision of the Market going forward for the next thirty years and beyond is key to turning around the business proposition. The physical shape and economic size of the Market is a key component of this strategic vision and will underpin any redevelopment of the Nine Elms site.

Of a number of business scenarios considered, redevelopment currently shows the highest net present value of free cash to Defra. This net present value is very dependent upon the assumed value gained for the site. This raises the issue of the method by which Defra realises the best value for the site as the uncertainty of the value in a redevelopment arises from the type of planning permission which can be achieved with the local Council. If Defra sells the site prior to gaining planning permission for a redevelopment there is the potential for purchasers to discount the value offered at the point of sale, only to realise an improved planning permission agreement following the sale and thus create a windfall gain. This could potentially be protected against by some form of gain share or overage, however these mechanisms can be limited in their effectiveness. A windfall gain could also be prevented through some form of joint venture or partnership but these options do not give Defra the complete disengagement it requires.

Our analysis points to Defra undertaking master planning prior to agreeing a strategic development brief with the planning authorities and before taking the site to the market. This would also allow for the Authority to feed in the requirements for the physical shape of the Market going forward based on a developed strategic vision. This would in turn be influenced by Defra's views about the extent of the Market facilities which it was intended to preserve going forward.

Until the development opportunity has been progressed, a final decision on the disposal methodology will need to wait. However, initial analysis points towards two separate transactions for the site and the Market to protect value for money.

With the abolition of the Authority through legislation, the Market business would need to be transferred to most likely a corporate entity. This entity could then be sold off through competitive tender, although it has to be recognised that there may be little or no interest in the Market business other than from the tenants.

The development site would then be sold through a competitive auction process. From the expressions of interest there are a number of potential bidders who would be keen to be involved in purchasing the Nine Elms site and it is important that this bidder community is managed appropriately to ensure a strong competitive process at the point of sale.

There are a number of important steps which Defra, working with the Authority, needs to undertake to prepare for any such disposal. The full analysis of these preparatory steps is outside the scope of this report. However, it will included preparation of an overall project plan and timetable; formation of a project team with allocated responsibilities; reform of the Market business; master planning of the Market site (including key decisions as to the proportion of that site to be allocated to the Market going forward, which presupposes decisions about the intended scope of the Market's activities); detailed financial analysis of the various options including the preparation of an outline business case; preparation of the necessary hybrid legislation, management of stakeholders, especially the tenants; and design of the disposal process itself.

1.Introduction

Defra has been considering future options for the Market for close to 20 years – most recently as joint sponsors of the 2002 Review of London Wholesale Markets conducted by Nicolas Saphir. Despite receiving wide acceptance for its recommendations, little progress has been made to implement the report's recommendations. Progress has been very slow due to a number of factors:

- A requirement for new legislation complicates a quick solution – the Covent Garden Market Authority was established by an Act of Parliament and is presently subject to four Acts of Parliament. Effective implementation of a material change in the nature of business undertaken on the market site at Nine Elms – as well as a complete change of ownership – will require a new act of (hybrid) legislation. In addition, we understand that the Corporation of London faces a similar situation with respect to modifying the nature of activities permitted at each of the London markets it owns.

- A desire to find a consensus solution – many parties have direct and/or indirect interests in the scale and pace of any future development of the New Covent Garden Market ("the Market") as well as London's other wholesale markets. The end result has been that there has been much discussion over the last 15 to 20 years but little real progress, particularly as some of the parties involved hold strongly differing views regarding the "best" solution.

- Lack of a strong and constant reason to change – until recently the market's facilities were of an adequate standard and the Authority was able to fund basic ongoing repairs and maintenance. This, combined with the fact that the Market largely pays its way in terms of day-to-day running costs kept the Market a low priority issue for the Department.

More recently, a number of factors have converged to renew Defra's desire to seek to disengage from the Market:

- The Market now faces an on-going capital expenditure requirement of circa £15 million - £30 million over a period of 15 years, according to estimates made by King Sturge and supplemented by the Authority. The Authority does not generate sufficient profits to finance this investment and Defra is unwilling to provide funding for this purpose;

- Central government departments are under increasing pressure to demonstrate efficient management of assets under their control. Whilst the Covent Garden Market Authority is a public corporation controlling its own assets, it remains ultimately responsible to Defra. Defra's role in relation to the Market is now seen as a historical anomaly with no basis in the new Department's published objectives. A recent review of the Department's activities has confirmed the long-standing policy that Government should disengage from the Market.

- Third parties are showing interest in the Nine Elms site and are seeking to create market interest for redevelopment of the site;

- Litigation resulting from a legal challenge by the Corporation of London, has rekindled the public debate around the range of permitted activities available to a London wholesale market; and

- The Market's future development is considered to be more a matter of London than national policy.

Remit and scope of work

For some years it has been the Government's policy to dispose of the market as a going concern and transfer both the business and the assets into other hands. PricewaterhouseCoopers has been appointed by the Department for the Environment, Food and Rural Affairs ("Defra") to provide advice on putting a disposal policy into effect.

Overall, Defra is seeking support in two areas: first, assessing and then marketing the opportunity for private sector (and possibly other) bidders to participate in the future development of the Market and its site; and second, setting up and managing the transactions which will be necessary to allow the Department to disengage from the market, the Authority to be wound up and for a market to continue in operation on a commercial basis. The S-Cat tender, proposed dividing the (potential) range of support required into three stages. This report provides our recommendations in connection with stage 1 of the work plan set out below.

Stage 1 – review of options and expressions of interest

The first stage was to involve two main tasks: first, the identification of options for transferring control of the market from the Covent Garden Market Authority to a private sector or other organisation independent of Defra which would be willing and able to maintain and develop the market business as a going concern; and second, to evaluate existing expressions of interest in taking over the market.

Advice in Stage 1 was to take account of all the considerations affecting a potential transfer of the market to a new owner, including:

- The financial position of the market and its tenants
- The planning policies and considerations affecting the future development of the site
- The future need for and viability of a market transferred as a going concern to a new operator
- Uncertainty as to the timing of legislation to wind up the Authority
- The possibility of interim solutions such as a joint venture between the Authority and a private sector funder

Output from Stage 1 was to establish which options justify further development.

Defra, in consultation with the Authority, would then decide whether or not the remaining work stages set out below should be taken forward.

Stage 2 – design and planning of the disposal process

The second stage is intended to focus on developing specific proposals for managing a competitive bidding process to secure best value for the taxpayer from the transactions involved. Consideration will also need to be given to the scope for interim arrangements, pending legislation, to enable the market and its site to be developed with the benefit of external financing prior to a transfer to a new owner.

Outputs from Stage 2 are to include recommendations on a critical path for disengagement from the Market whilst preserving the market operation as a going concern.

Stage 3 - implementation

The third and final stage is to involve implementing the plans produced in Stage 2 (if Defra so decides).

By the end of Stage 3, secure arrangements should be in place for the future financing of market facilities which reflect the needs of a sustainable market, are affordable and appropriate to tenants' needs but which do not impose costs on the taxpayer.

Out Approach

Our approach involved the following:

- Developing a sound understanding of the underlying business and the markets in which it operates through:

  - The conduct of 30 semi-structured interviews with a cross section of individuals representing the broad range of direct and indirect interests in the future development of the Market. Our sample included representatives from Defra and the Market Authority; flower, fruit & vegetable and catering distribution tenants, as well as interested third parties ranging from the local Borough Councils to Nicolas Saphir, the Corporation of London, industry associations and the Shareholder Executive. (A full listing of individuals interviewed can be found in Appendix C.)

  - A review of previous reviews / studies relating to the future development and / or disposal options for the Market, including Nicolas Saphir's 2002 Review of London Wholesale Markets as well as Counsel's opinion on the legal and practical implications of the guidance set out in the existing legislation for both Defra and the Market Authority.

- Review of performance and management reports for the Authority including current and historical annual financial statements, management accounts/budgets, tenancy and service charge agreements, capital expenditure plans and site development plans. This work highlighted that the Market was not operating on a long-term commercially viable basis. In particular, that the Authority was not able to self-finance the required level of capital investment combined with Defra's decision not to provide capital funding would mean that further decline in the condition of the market's infrastructure was inevitable. As a result, it was judged necessary to assess different business scenarios alongside potential disposal options. In brief, the scenarios considered were:

  1. **Status quo** – Developed to provide a baseline for comparison of alternative scenarios. The Covent Garden Market Authority currently produces only annual budgets and therefore it was necessary to develop illustrative projections using available historical data and a number of assumptions discussed and agreed with the Authority management.

  2. **Reform** – An illustration of the range of operational changes and additional capital investment that could be undertaken to put the Market on a financially viable and self-sustaining footing. This scenario was developed for two main reasons: first, to gain an understanding of the nature and scope of changes necessary to make the business viable and, second, to assess the implications of existing tenancy and service charge agreements on the timing of reform and the degree of flexibility available to the Authority (or any future owner) for implementing change.

  3. **Closure** - Market closure followed by wholesale redevelopment of the site at a future date. This scenario was developed to provide another baseline for comparison and to explore the financial implications for Defra should the other scenarios fail and this become the default option.

  4. **Reform and redevelopment** – Reform of the business together with partial redevelopment of the site. In the absence of a full master planning exercise, this scenario focuses on a very specific example of how the site may be reconfigured, i.e. the most recent GMW proposal. This enables us to assess the viability of redevelopment in some form. However, it is recognised that a range of other reconfigurations may be more appropriate and financially attractive.

- Working with Defra representatives to identify and agree both the criteria to assess these scenarios as well as the disposal options proposed.

- Working with representatives of the Market Authority to develop illustrative financial projections and agree the assumptions underpinning those projections related to the above scenarios considered. In developing these projections we sought as far as possible to build on recent financial reviews conducted by PKF and others. We point out that the projections developed were intended as illustrations of some of the possible future development paths for the Market. They are cash flow based projections designed to explore the financial implications of each scenario, including an indication of its possible net present value on a simple discounted cash flow basis. They are not intended to serve as tools for on-going business planning or management of the Market. (Please see Appendices A and B for the data book setting out the assumptions developed and applied for each scenario as well summary analysis pages for each scenario assessed.)

- Developing a list of disposal options available to Defra for disengaging from its Market ownership role.
- Looking at different approaches to the disposal (rapid; or with more preparation); the disposal methodologies and mechanics; possible options available in the absence of legislation; and possible transfers within the public sector.

Our work was conducted over a 14 week period from mid-June 2005 to late September 2005.

Outline of report

The rest of the report is structured as follows:

- Section 2 provides a brief overview of the Market, its tenant base and recent performance and industry trends.
- Sections 3-7 provide summaries of each of the business scenarios considered and of our quantitative and qualitative assessment.
- Section 8 outlines the disposal approaches available to Defra.
- Section 9 analyses disposal methodologies
- Section 10 covers the Expressions of Interest received

The report has the following Appendices:

A Authority Projections and Data book

B Financial Model Output Sheet

C List of interviewees

D List of publications

E Expressions of Interest

2. Market Overview

Disengaging from ownership of the New Covent Garden Market is unlikely to be a straightforward process due to Defra's requirements for disengaging (both statutory and policy-driven) as well as the wide range of stakeholder groups who need or may seek to be involved in this process. This section distils what we consider to be necessary background information on the Market's principal businesses, the markets in which they operate as well as the current state of the wider debate regarding the future of all of London's wholesale markets. It contains a summary of some of the common themes shared during the course of our conversations with market traders and other interested parties.

The underlying market business

Based at Nine Elms near Vauxhall since 1974, New Covent Garden Market is the largest horticultural wholesale market in the UK, covering 56 acres. It is operated by the Covent Garden Market Authority, a public corporation established under the Covent Garden Market Act of 1961 and governed by subsequent Acts of 1966, 1969 and 1977. The members of the Authority are appointed by, and the Authority is responsible to, Defra Ministers.

Market traders operate within two primary sectors – fruit & vegetables (both wholesale and catering distribution) accounting for roughly 70% of the Market's turnover in 2003/4, and flowers (15% of turnover). The remaining 15% is generated via non-horticultural food activity[1]. Over 250 tenants operate within the Market, providing employment for roughly 2,600 people.[2]

The following section reviews some of the major trends in each sector and views/impressions based on the interviews held with market traders. This section reports information and personal views shared during interviews with market participants. We believe they provide an accurate summary of their perceptions regarding the Market and the industry overall but have not verified the views or facts provided.

Fruit & Vegetable and Catering Distribution market trends

The UK wholesale market for fruit and vegetables has experienced significant growth in recent years, with fruit and vegetable sales by wholesaling businesses in 2004 expected to be 26% higher than in 2000 implying a compound annual growth rate of 6.5% for this segment of the wholesaling market.[3] However, the growth of the supermarket industry means that wholesale market traders will have experienced limited benefit from this. The growth in the number of catering distributors located at the Market reflects a national growth trend in the foodservice industry. The fruit and vegetable wholesalers located at the Market sell 70-80% of their produce to catering distributors who are also based within the Market. The remaining sales are made to local independent retailers, although this segment of the market is

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[1] Source: Covent Garden Market Authority management accounts

[2] Source: Covent Garden Market Authority [publication/website]

[3] Mintel "UK Wholesaling and Cash and Carry 2005", (includes cash & carry and delivered businesses) page 14

declining.[4]

After several years of rapid growth in this sector, current estimates suggest that growth will stabilise and may even start to decline[5].

The catering distributors at the market benefit from the close proximity of the wholesalers, and the strongly competitive environment within the wholesale area, which results in lower prices. The main threat facing the catering distributors is from competitors who are able to offer a 'one stop shop' and supply other non horticultural produce.

What we heard – impressions from fruit & vegetable trader and catering distribution interviews

The 1980s saw the rise of the supermarkets and the disappearance of much of the Market's traditional client base, including independent retailers and green grocers. This was further compounded by the loss of a large portion of the business catering market to integrated suppliers such as Compass, 3663 and Brake Brothers.

After a number of difficult years which saw the demise or exit of many traditional wholesale operators from the Market, the 1990s saw a reversal in fortune. A prolonged period of strong economic growth combined with a growing consumer trend towards eating out resulted in a new source of demand suited to wholesale markets, namely catering distribution. This focused largely on supplying high quality fresh and/or lightly processed fruit and vegetables to the central London restaurant and hotel sectors.

Interviews revealed an underlying tension between some of the catering distributors and the more traditional wholesale traders over the likely path of future growth.

- On the one hand, the Market has undoubtedly played an important role as a business incubator for many of the new catering distribution companies. For example, catering distributors benefited from being able to source their supplies from a single location that provided a broad range of high quality produce, where suppliers were subject to a healthy level of competition (price, quality and availability). This allowed efficient consolidation of an often varying quantity and mix of products at competitive prices. In return wholesalers have a relatively constant source of demand although they continue to bear the risks/costs of spoilage and/or of not being able to clear their supply on any given day.

- Additionally, market traders and other commentators (including Saphir) expect that catering establishments will increasingly want to collect as much of their supplies as possible from a single location and/or have their supplies delivered in as few vehicles as possible.

- On the other hand, however, a number of catering companies indicated that their future growth plans were unlikely to involve Market based operations. The prime reason provided for seeking alternative locations was a limited degree of "operational fit" between their standard catering supply offering and their planned higher value services. Factors mentioned include:

    - Risk of the new operations interfering with the workflows of the existing operations, or vice versa. Interviews typically indicated that modification of current facilities represented a second best option to leasing a new purpose built facility.

    - Need to meet more demanding health and safety standards required by higher value processing and/or greater levels of customisation of their supply capabilities and operations (including consumer/ general retail offerings). While present facilities could in theory be upgraded to the required standards, respondents felt that a more modern or purpose built site

[4] Interviews with Covent Garden Market Authority and market traders

[5] Source: PwC analysis of New Covent Market Garden annual sales data. Note: 2004 figures are initial Market estimates and may change.

could offer these facilities on a more timely and economic basis.

- Market location, combined with limited/difficult access for the general public, a shortage of suitable parking spaces as well as the wholesale market's hours of operation were not conducive to supporting a retail operation.

Flower market trends

The national market for cut flowers and pot plants has grown by 60% over the 5 year period 1999 to 2004 (with annual sales in 2004 estimated at £1.5bn)[6]. While the latest (2004) turnover figures from the Flower Market show a 4.7% increase in sales volume in that year, traders at the Market have in the main and more recently experienced a decline in sales and shrinking profit margins. This is primarily due to the entrance of supermarket chains into the market, which have increased their market share from 20% to 62% since 1995, as well as the impact of alternative supply channels including pack houses and (independent) overseas suppliers. As a result, the market share of traditional wholesalers has shrunk from 44% to 24%.[7]

What we heard – impressions from flower trader interviews

Interviews suggest that traders face a range of issues from succession planning to longer-term financial sustainability to increasing competition from new forms of distribution combined with more traders competing for the remaining but declining customer base.

All the traders we spoke with related similar experiences in terms of the significant impact on their traditional wholesaling businesses resulting from the growth in and expansion of the supermarkets into flower and garden supplies combined with the subsequent growth in pack houses to serve the supermarkets. These shifts in demand, combined with the on-going growth in the volume of trade captured by what has come to be known as the "Flying Dutchmen" have resulted in a significant decline in their traditional customer base over the last 20 years. While not new, the base of largely independent operators, have developed an efficient order collection and delivery model based on buying a limited range of products "on the clock" at the Netherlands flower auction and then providing a convenient, reliable, low cost, door-to-door delivery service to UK florists, small retail shops, green grocers and in some cases the general consumer. UK operators have found it difficult to compete with these small operators due to a lack of financial resources as well as the (relatively) high costs of sustaining their own overseas buyer/driver.

One result of this trend appears to have been that Market flower traders diversified into supplying niche markets much earlier than the fruit and vegetable traders operating on the same site. Interviews indicated that one of the main remaining strengths of the traditional wholesalers lay in their abilities to provide both variety and reliability when meeting complex and/or specialist demands for often exotic flower varieties that are typically imported from overseas. Due to their early move into supplying pockets of niche demand we understand that many flower traders have developed strong personal relationships with clients based on reliability and trust rather than price, which is proving an effective barrier to price-based competition of the Flying Dutchmen.

Interview participants indicated that the decline experienced at the Market in recent years appeared to be stabilising.

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[6] Mintel – Houseplant and cut flowers, Market Intelligence, September 2004

[7] Mintel – Houseplant and cut flowers, Market Intelligence, September 2004

What we heard – impressions on the tenant base from interviews

All traders commented that volumes and profits were in decline. As most market trading operations are private businesses they are not required to publish detailed annual accounts making it difficult to verify the claims made. That said, we were able to review a limited sample of accounts for traders operating at the Market which offer some support for their claims. Based on a limited sample we found that for 2003/04 fruit and vegetable traders reported average gross profit margin of 17% and an operating profit margin of 1.4%. Unfortunately, we were unable to find a sample of published accounts for flower traders.[8]

The tenants we spoke with indicated that market morale has been negatively impacted by the significant, on-going uncertainty surrounding the future of the site. This negative sentiment has been intensified by speculation following recent reports and expressions of interest and is a cause for concern and frustration for both tenants and employees alike.

Apart from the commercial interdependencies created through trading with one another, there is little or no experience of the tenants working together. The Market represents a grouping of individual business undertaking a common trade.

Market traders have adapted well to the evolving supply and demand dynamics in their respective markets. The solution for both segments has involved adapting to new, typically niche, sources of demand. In addition, some flower traders have been able to continue to benefit from their strong personal relationships with a range of demanding but loyal clients for whom reliability and quality are more important than price.

Finally, we noted that in almost all conversations with market participants – including the Tenants Association – the fact that flower wholesaling is typically mentioned as an afterthought, if at all, when discussing the Market and its future. Even the recent Tenants Association / Saphir proposal only mentions this segment in passing and makes no substantive suggestions as to how the proposed plan will contribute to the long-term benefit of these traders.

Market operations

Rental income

We have received some information suggesting that Market rents are currently below market rates for light industrial units in the surrounding area. According to a report on employment land and premises commissioned by Wandsworth Council[9], industrial rent levels in Wandsworth are among the highest in London, with rents for new units around £11 - £12 per square foot[10][11]. The average rent of the trading areas is approximately £6.60 - £6.92 per square foot and approximately 40% below open market rates. Although lower rents would be expected for the present facilities given the specialised nature of the units, their age and the growing need for repair, current rents appear low. Substantially re-conditioned or new facilities would command higher rents.

Lower rents may be some compensation for the service charge which the Authority considers to be higher than those in the surrounding area. However, we estimate that the Authority only recovers approximately 55% of its total expenditure from the tenants via the service charge and direct recoveries. A substantial

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[8] Source: Sample of annual accounts for 4 companies submitted to Company's House for 2003/04

[9] The Future of Employment Land and Premises in Wandsworth, Roger Tym & Partners, November 2004.

[10] Source: King Sturge, quoted in The Future of Employment Land and Premises in Wandsworth, Roger Tym & Partners, November 2004.

[11] The report refers to rent in terms of square feet as this is the dimension used by the Authority when setting rents and used in the report quoted.

portion of the un-recovered element is made up of non-operational expenditure which is not charged to tenants based on the Authority's interpretation of the Service Charge agreement. Of operational expenditure, the Authority estimates that some 75% is currently being recovered, the shortfall being accounted for by vacant premises on which service charges are not levied. As the rents and service charge income do not cover all of the Authority's costs, the Authority must look for other income sources.

Approximately 108 leases expired in April 2005, of which 91 were not protected by the security of tenure clauses of the Landlord and Tenant Act 1954. The authority did not seek to discriminate between protected and unprotected leases and therefore did not seek to establish whether it was possible to set a higher rental tone for the renewed leases. Apart from new lettings in the meantime, rents will not be subject to review until 2010 when the majority of the leases expire.

The Authority currently provides market facilities to approximately 250 tenants under approximately 400 leases. In terms of total area available for letting to core fruit and vegetable and flower market activities, including office space, the market has an overall occupancy rate of 81%. Trading unit occupancy is higher at 91% for the fruit and vegetable market and the 88% for the flower market. Office occupancy is much lower at just 44%. Authority management expect that the flower market may see a 5-10% fall, while occupancy of trading units is expected to continue at current levels.

This is significant for two key reasons:

- Additional rental revenue would be generated on a site with higher occupancy rates
- In accordance with the terms of the current service charge agreement, the authority covers the charges falling to the vacant units and offices, resulting in low cost recoverability overall.

Service charges

In addition to providing the physical market infrastructure, the Authority also provides a range of services to its tenants including utilities, security, cleaning and waste disposal. The costs of providing these services are recovered from the tenants, either directly in the case of metered electricity and water, temperature control or catering processor waste, or via the General Service Charge (GSC).

The GSC comprises a basket of running costs and some the non-core revenues generated by the Authority, e.g. commercial vehicle receipts. The GSC per square foot is calculated based on the total trading and office area available to let and as noted above, the Authority then covers the void areas (circa 10% of trading units and 56% of offices).

The basis for calculating the service charges is defined in the terms of the lease agreements and the underlying principles have remained unchanged since 1978. The terms of the service charge are somewhat unusual in that they place an emphasis on the accounting treatment of particular items of expenditure. As a result, the decision whether to recharge costs to tenants is influenced more by the Authority's accounting practices rather than the practices of a (commercial) landlord.

We note that Defra and the Authority are currently examining the interpretation of the GSC provisions. The matter is being reviewed by their respective legal teams with a view to reaching an agreed position regarding their application. Whatever the outcome, it is clear from analysis of the Authority's annual accounts for the 5 financial years from 2000-01 to 2004-05 that the Authority only recovered between 54%-58% of total pre-tax revenue expenditure (i.e. staff costs, operating costs and depreciation). It is also clear from analysis of the scenarios below that in order to reform the business and improve its longer-term commercial viability, greater recoverability of costs is needed, whether by broader interpretation of existing terms or revision of the lease provisions.

Maintenance expenditure and capital investment

It is noted that some tenants have made substantial investments in their individual units but it is estimated by the Authority and King Sturge that in the order of £15 million to £30 million of capital investment is required over the near term to ensure that appropriate infrastructure standards are maintained, and that facilities and services are suitable to enable the Market to meet its statutory obligations.

This maintenance and capital expenditure back log has arisen over a number of years due in part to the insufficient profits generated from market operations to finance the work and in part to the Authority surrendering a large proportion of its annual surplus to Defra. Under section 44 of the Covent Garden Market Act 1961, as amended by the 1977 Act, the Minister may direct the Authority to pay to him (a) the whole or part of any excess of the revenues of the Authority for any accounting period or (b) any amounts received by the Authority otherwise than by way of revenue. This practice continued until around 2000, from when Defra allowed the Authority to retain its surplus to finance at least part of the maintenance backlog.

As the estate has aged, the nature and scale of investment has increased – £6 million replacement of the roofs in 2004 is most recent example – the surplus generated has been insufficient. In order to fund the roof repairs, the Authority used some of its reserves. In 2004-05 and 2005-06, Defra committed to fund £1.675 million works required for health and safety reasons. There are no plans to make further funding available as the Market is not central to the Department's policy objectives.

We have been informed by Authority management that further significant delays in making the necessary investments increases the risk that the Authority could fail to meet some of its statutory duties with respect to the provision of adequate market facilities.

Financial Performance

Review of the audited Authority financial statements for the years 2000-01 to 2004-05 shows that the Authority has regularly met its statutory duty to at least break even taking one year with another.

Income from the Market premises has increased steadily since 2000-01 except for a 6% fall in rental revenue in 2002-03 due to a fall in office occupancy from 60% to 50% of available space as wholesale traders increasingly chose to base their administrative functions within their units. Rental income has since recovered although occupancy rates remain constant.

Profit Margins

Between 2000-01 and 2004-05, the Authority's operating profit fell from £1.9m to £1.1m in spite of growing rental revenues. During the same period, operating profit margins fell from 22.7% to 10.0%, with a further fall to 7.3% projected for 2005-06 based on the Authority's management accounts.

This downward trend in profitability reflects a basic rigidity in the underlying economics of the business resulting from the nature of lease and service charge agreements currently in place. In particular, while the proportion of costs recovered from tenants has remained constant, the total cost base has continued to increase and at a greater rate than rental increases. As a result, profit margins have fallen.

Returns on Capital Employed

The return on capital employed, measured as profit before interest and tax over average total net assets, has fallen over the same period. We estimate that in 2004-05 the Authority generated a return of approximately 7% on its average capital employed compared to almost 15% in 2001-02. This fall is consistent with the Authority's falling profits. The decrease was even greater because of the substantial capital work undertaken on the Market roofs and the resulting increase to the value of the Authority's asset base.

Moreover, these returns are calculated on an historic cost base. In accordance with section 46 (2) of the 1961 Covent Garden Market Act, the Authority prepares annual accounts in a form directed by the Minister, with the approval of the Treasury. It is directed by Defra to adopt the historic cost accounting convention [12] and therefore the Authority's fixed assets are stated at professional valuations as at 1 April

[12] Authority Accounts Direction issued by the Minister. The latest Direction was agreed in 2003.

1977 plus subsequent additions at cost, less disposals and accumulated depreciation. The current value of the Authority's fixed assets is likely to be much greater than its historical value. Therefore, if the current value could be reliably estimated, a much lower return on capital employed would result. It is clear that even under the historic cost accounting convention, the Authority does not generate high returns or sufficient profits to self-finance its investment needs.

The Authority prepares an annual budget for approval by the Board but has adopted a less systematic approach to longer-term business planning. We understand that it does not produce a long-range business plan as a matter of course. A capital investment budget was prepared in 2001, providing a high-level breakdown of expected capital expenditure for the period to 2006-07 and an updated 3-year programme of capital expenditure has recently been prepared.

We understand from the Authority that due to the uncertainty over the future of the market and the expectation of imminent disposal or closure during the past 15 years, it considered that normal long-term planning processes were rendered impossible and pointless. However, it is likely that a more commercially-orientated business would have continued to undertake longer term business planning (i.e. for more than one year) until such a time that a decision was actually announced and implemented.

Previous studies

A number of previous reports have been commissioned by Defra to consider the future of the Market, most notably the 'Review of London Wholesale Markets' (Saphir, 2002) which had a wider remit to consider all wholesale markets in London. This report and its recommendations still provide a helpful overview of the current state of the debate regarding the future development of the London wholesale markets. Given the interdependencies between the future development of Covent Garden Market and the wider London markets debate a brief summary of the report is set out below.

Saphir's Remit

- Whether the existing London wholesale market facilities are well adapted to the needs of the business communities and users they serve
- Effect of governing legislation on the operation of the markets
- The potential impact of product diversification and changing demand for the services provided by the wholesale markets
- The scope for developing a co-ordinated strategy for the future management of the markets

Future Ownership and Management of Markets

Saphir concluded that markets continue to provide some remaining 'public good' which warrant a degree of ongoing support:

- Wholesale markets provide new immigrants with a starting point for their economic establishment within society;
- Reduction of traffic congestion in central London by consolidating trade, thereby allowing improvements in the integrated management of inward supplies and outward distribution;
- Larger markets would allow for more economic inspection services
- Improved waste management through the consolidation of preparation facilities on large composite sites.

Other conclusions included:

- Markets should offer a full catalogue as well as additional services to the catering trade, e.g. laundry, marquee and temporary catering hire, menu printing and ice supplies, vehicle maintenance and rental, cold storage maintenance, catering equipment supplies, specialist staff recruitment for whole catering trade, skills training centre.

- Development into 'higher risk' foods, added value and preparation raises longer term question of the overall hygiene conditions of the Market. The poor state of the buildings, the condition of some of the facilities, particularly under the railway arches and longer term re investment issues, as well as legal constraints, act as a brake on the full development of the site. Saphir saw the future as a general catering food service centre for London.

- As the markets become less like markets and more like others in the supply chain, the burden of site investment and management should pass increasingly to commercial providers.

Saphir's Recommendations

- Rationalise and consolidate the markets to increase competition.

- Remove restrictive legislation to improve effectiveness of the supply chain.

- Three composite markets for meat, fish, fruit and vegetables based at the sites of Nine Elms, Spitalfields and Western International.

- Reduce traffic congestion by improving distribution efficiency (integrating collection and increasing drop size). (According to the Authority website, 4,500 vehicles enter the Nine Elms site daily, rising to 7,000 at peak times.)

- Develop separate dedicated areas for retail markets at certain times of the week. Potential for on-site Farmers Markets.

- The report did not recommend the establishment of a central planning, management or liaison body for London markets to bring about and regulate change, preferring the removal of legislation that restrains trade and allowing competition between markets to establish competitive efficiency.

Covent Garden Market specific studies

In addition to the Saphir report, a number of studies relating specifically to the Market have been undertaken. The first of these studies, in 1989 by BDO Binder Hamlyn, considered the privatisation options available to DEFRA. In 1994 and 2002, Knight Frank considered the disposal potential of both the land and buildings and in 2004 GMW Architects generated a development proposal to support the Saphir review. Earlier in 2005, PKF undertook a financial evaluation of the Market and Authority.

Key points for future analyses

Underlying market trends in the market business overall

- The evolution of market activity towards serving ever narrower (or "niche") pockets of demand reflects the fact that wholesale markets are playing an increasingly peripheral role in the overall supply chain. While they can still be said to play a significant supply function for local markets as well as small food and catering businesses, the fact they play an ever decreasing role in balancing supply and demand makes them of less strategic importance for farmers and growers.

- That said, there are a number of factors in favour of the current business model including an expectation that catering establishments will:

  - increasingly want to collect as many of their supplies as possible from single locations or have their product delivered in as few vehicles as possible; and,

  - continue to look for ways to reduce unnecessary preparation in the kitchen. This trend of prewashed and peeled supplies is expected to be reinforced by the economics and environmental advantage of preparing and semi-processing in larger batches.

- The Saphir report and other research sources suggest that markets will need to adapt to adapt to new technologies, e.g. the internet. However, we understand that past efforts by the Authority to engender interest amongst its tenants for internet-based trading have been largely unsuccessful.

- Interviews with Market tenants as well as market research point to continuing pressure from supermarkets, packhouses and the 'Flying Dutchman' making it difficult to anticipate a buoyant future for the wholesale flower trade.

Health of the underlying tenant base

- Tenant profitability/financial strength is very difficult, if not impossible, to accurately assess as tenants tend to file abbreviated accounts which provide very limited disclosure to third parties. This is in accordance with small business reporting rules and practices, but does make it more difficult for the Authority to judge the impact of any proposed rent or service charge modification on the tenant base. While not conclusive, our initial review of a small sample of published accounts does, however, indicate that operating margins for catering distribution firms appear to be modest.[13]

- However, in situations of high multi-occupancy investments, monitoring of the tenants covenant strength is often seen as less important, as the cash flow is supported by a portfolio effect. In these situations, the landlord and property manager's emphasis is on keeping occupancy rates at a high steady rate. Consideration should be given to covenant or portfolio enhancement where the tenants carry on similar trade as they may be subject to sector decline (this could be case for New Covent Garden Market).

Finances of the Authority

- The Authority is both profitable and cash generative. At the moment, though profitability has declined it does not generate sufficient cash to allow for the scale of repairs and maintenance needed.

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[13] Source: Sample of annual accounts for 4 companies submitted to Company's House for 2003/04

3. Business scenario review

Summary of scenarios considered

In this section we examine a number of scenarios for the future of the Market business, all of which are in principal neutral with respect to who owns it. They range from the status quo to market closure which are both analysed simply as limiting cases. We also consider two scenarios for improving the core business by operational means, one of which offers a partial redevelopment of the site. The scenarios in more detail are:

- Status quo – the market business continues as per current plans and projections.
- Reform – a combination of measures are introduced to create a sustainable business. The scenario considers the impact of increased rents, improving the recoverability of market running costs through a reformed service charge and refreshing the Market infrastructure. The scenario aims to assess whether better value may be achieved in the longer term by reforming the business in the short-term.
- Closure – the closure of the market followed by wholesale redevelopment of the site is examined.
- Reform and Redevelopment – steps are taken to create a commercially and financially viable business and partially redevelop the site. We recognise that the scenario uses a highly specific example of how the site may be redeveloped and there may be other more appropriate reconfigurations, nevertheless, the scenario aims to demonstrate whether redevelopment in some form is viable.

The scenarios have been assessed taking into account both quantitative and qualitative considerations.

The reason for considering the scenarios is that Defra has an objective that the Market should continue as a going concern post disposal. It is necessary, therefore, to consider the pre-conditions for the Market's continuing to operate as a going concern (and, in particular, any reform measures needed); and how they could be satisfied in the context of a disposal.

The scenario analysis has been carried out in the context of Defra's policy objective of seeing the Market continue as a going concern. Scenario 3 (closure) would be inconsistent with that objective and has been considered only as a theoretical limiting case. The scenario analysis is not therefore intended to be used as an aid towards decision making between closure and other options. It would not in any case be suitable for that purpose since (as explained in more detail below) there are very significant uncertainties surrounding the financial impact of all four scenarios, particularly those involving disposal of all or part of the site (i.e. scenarios 3 and 4). If Defra wished to consider the closure option in its own right, this would require further detailed study. Similarly, any disposal option which required the application of public funds would require separate justification through the preparation of an Outline Business Case.

The quantitative analysis has been carried out using a model of the Market, based on historical data and forecasting assumptions provided by the Authority's management and data from previously commissioned reports. The assumptions are set out in Appendix A. We have not verified this data or the assumptions. We have only considered the costs listed. The model is not a full investment appraisal and therefore some potentially material costs may not have been considered, for instance the costs of decontaminating the site. The model is a cashflow model which analyses the economics of the scenarios considered in Net Present Value (NPV) terms. It does not consider financeability. Accordingly, the outputs from the model are suitable for giving illustrative support to quantitative analysis of the scenarios. They should not be relied on as the basis for investment decisions.

4. Scenario 1 – Status quo

Overview

This scenario provides a baseline case against which other scenarios can be assessed, quantifying current operational performance and profitability. The Authority does not prepare a long range business plan, so this scenario demonstrates the need for change by analysing the financial impact if current business practices continue.

This scenario assesses the financial health of the business and its ability to generate profits if no action is taken to change its current business model and occupancy of units remains flat. It also looks at the financial impact of undertaking a significant maintenance and repair programme.

The following key assumptions have been made:

- The core business of providing trading and office premises to small- and medium-sized businesses will continue. Tenants will continue to pay rental and service charges, and the Authority will only aim to break even so that revenues are sufficient to meet all expenditure chargeable to its revenue account, i.e. profit and loss account.

- It is assumed that occupancy of trading units and offices remain at March 2005 levels of 90% and 44% respectively. Tenants leaving the market will be replaced by new tenants on the same rental and service charge terms and conditions.

- Current rents are calculated using the analogue formula and are fixed, except for a 5% step increase in the final year of the lease, until the majority of leases are renewed in 2010. It is assumed that the Authority does not attempt to set a higher rental tone, i.e. charge higher rents, for new lettings before 2010 and therefore the Authority does not increase rents on renewal of existing leases to reflect prevailing rates in the local area.

- In the three year period December 2000 – December 2003, industrial rent values in Wandsworth rose by 5.0% per annum, more than twice the average rate for London (2.3% p.a.) or the UK overall (1.9%)[14]. Given the specialist nature of the site, it is assumed that rents will increase in line with RPI inflation each year after 2010.

- The basis for recovering service costs is fixed until the majority of leases are renewed in 2010. Thereafter, it is assumed that the service charge terms remain unchanged, with the calculation being based on revenue expenditure published in the Authority's financial statements and defined in accounting rather than surveying terms. The Authority will continue to cover the service charge falling to vacant units, i.e. 10% of trading units and 56% of offices.

- This scenario assumes that the majority of tenants are protected by the terms of the Landlord and

[14] Source: Investment Property Databank, quoted in The Future of Employment Land and Premises in Wandsworth, Roger Tym & Partners, November 2004.

Tenant Acts and the tenants exercise their rights to block any substantial changes to rents and service charges in the future.

- This scenario considers two positions regarding investment in the fabric of the infrastructure. We look at the impact if only the 2005-06 capital expenditure budget and the 3-year maintenance programme proposed by the Authority are undertaken. We also examine the impact of following the ongoing maintenance programme proposed by King Sturge[15] thereafter.

- There is no additional financial support from Defra or other body.

The potential impact of more stringent environmental or health and safety requirements have not been taken into account.

Quantitative assessment

In order to fulfil its statutory obligations under section 37 of the Covent Garden Market Act 1961 as amended by the Covent Garden Market (Financial Provisions) Act 1977, the Authority must secure revenues that are sufficient to meet all sums charged to its revenue account taking one year with another. On this analysis the Authority would continue to meet this statutory duty and break even in revenue terms if the status quo were to continue. However, the Market would generate insufficient profits to maintain the fabric of the market.

Cost recoverability via the service charges and direct recoveries would remain at current levels of approximately 55%. So costs would continue to be cross-subsidised from both the rents and third party revenues. This means the rents paid by tenants would actually be lower than the headline rate as a proportion covers the service charges falling to vacant units. By continuing to follow the current business model, the Authority would not generate sufficient surplus funds to meet either its planned capital programme or the King Sturge proposed works thereafter.

There will be no additional funding from Defra to meet the capital investment. Providing financial support to the market is not in line with Departmental priorities and it would represent state aid as it would distort, or threaten to distort competition in the provision of light industrial units. Although unlikely, such state aid could be challenged by the European Commission.

Without investment, the assets supporting the business will continue to deteriorate. The repair and maintenance costs needed to address the decline will continue to grow. A deteriorating asset base will also impact on the Authority's ability to secure lettings and charge RPI-increased rents.

As noted above, we have modelled two positions over a 15 year period. The first includes only the Authority's estimates for capital and maintenance costs over the 4-year period to 2009 and results in a positive NPV of £7.3m. However, the Authority would have to carefully manage the negative net cash outflows from this limited short-term capital expenditure and this position takes no account of the deteriorating asset base in the longer term.

The second position includes the ongoing maintenance programme proposed by King Sturge and results in a negative NPV of £0.3m. This indicates an unsustainable position and gives no protection against any revenue downturn or cost overrun.

Allowing the status quo to continue without any reform of the business not only fails to generate value in terms of market operations but also negatively affects the disposal value of the site and the long-term existence of the markets. With an incumbent tenant that cannot demonstrate its long-term viability, any potential buyer will offer much less for a site and Defra would be able to secure only very general assurances and limited contractual safeguards over the continued operation of the markets.

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[15] Planned Preventative Maintenance Programme of NCGM for DEFRA, King Sturge, March 2005

Qualitative assessment

Although maintaining a wholesale Market at Nine Elms is consistent with the wishes of most stakeholders, the long-term sustainability of the Market would remain questionable without significant capital expenditure and the status quo does not generate sufficient profits for the inward investment needed.

There is concern among the current tenants over the Market's future, brought about by the decaying infrastructure, financial anxieties, the frequent reviews by Defra and the legal challenge currently preventing face-to-face trading in fish and meat at the Market. Such concerns will remain and intensify if the market continues in its current form given that it is not a viable business for Defra or any other third party in its present condition.

In recent years, occupancy of trading units and offices has fallen. Not addressing the decaying infrastructure risks creating a negative spiral whereby continued uncertainty over the Market's future reduces tenant morale further and places further financial pressures on the Authority.

As well as the internal market environment, significant impacts would be made on the local external environment. With over 2,600 employed on the site or operating as sole traders, the eventual demise of the market would have a significant effect on local employment.

Conclusions

Our analysis suggests that the Market is not operating on a long-term commercially viable basis. Tenants pay below market rents and the service charge does not cover a significant proportion of running costs. Unless current management practices change, the Authority will not be able to turn around the business. As a result, the Market will continue to generate a low return and will be unable to fund the significant financial capital investment required to maintain the facilities at appropriate standards. Low returns will also constrain the Authority's ability to redevelop the market.

As a result it is unlikely that the Market in its current form would be considered as either an attractive or commercially viable business proposition by a private sector investor. However it is clear that the Market has valuable core assets such as its property base, established network of suppliers and clients, and its brand name/reputation which suggest that commercial value could be generated in the long term, subject to additional investment and business development.

Further decline of the Market is inevitable unless capital is invested in the infrastructure of the Market. This scenario is not considered sustainable in the long term.

5. Scenario 2 – Reform

Overview

This scenario examines the nature and scale of reform possible within the constraints of current legislation that would enable the Market to become financially sustainable and to self-finance the capital investment needed to refresh and maintain the market facilities. In particular, we consider the impact of increasing rents to open market rates and recovering a higher proportion of running costs.

The following key assumptions have been made:

- The core business of providing trading and office premises to small- and medium-sized businesses will continue.
- Changes to the business will be limited in the short-term as the existing leases and service charge agreements are fixed until the 31st March 2010. Nevertheless, reform of business practices and procedures should begin as soon as possible.
- It is assumed that the Authority adopts a higher rental tone and increases rents from the 1st April 2010 to an open market rate of £10 per square foot, based on a report by the London Borough of Wandsworth[16]. This assumed level of rent would need to be tested and viewed against the background of ageing facilities. It is recognised that the Authority would need to provide a higher level of service, which might require levels of refurbishment beyond those assumed in this scenario, in order to command higher rents.
- It is assumed that occupancy of trading units increases from 2007-08 onwards on the basis that a favourable decision by the House of Lords (following their judicial review of face-to-face meat and fish trading) and new 10-year leases (with break clauses) attract new traders or further investment by current traders. Trading unit occupancy will increase to 95% in 2007-08 and 98% in 2008-09. These new lettings for the period to 2010-11 will be charged at £7 per sq ft., and thereafter at open market rents.
- The offices are let to a core of tenants and occupancy rates are not expected to increase. However, in order to minimise costs, the offices will be reconfigured so that where possible tenants are grouped together in one area.
- The Authority follows the comprehensive programme of maintenance and repairs as proposed by King Sturge to ensure that adequate facilities are provided and to attract and retain tenants, particularly in the value-add sectors. The capital expenditure will be met by the increases in rents and service charge. The £4.5 million[17] funds held by the Authority may be used to alleviate any

[16] Wandsworth Employment Land Study, Roger Tym & Partners and King Sturge, November 2004

[17] According to Authority Board Paper AP/05/27, the Authority's investments at 30th June 2005 amounted to £9.3m. £6m was in respect of the Market Account and £3.3m of the Market Towers Contingent Liability Fund. The Authority's Finance Manager estimates that funds in respect of the Market Account will fall to around £4.5m once the 2005-06 insurance premium and other

cash flow difficulties before rents can be increased. With an updated and improved infrastructure, the Market could also benefit from lower maintenance costs.

- No legislative change will be necessary to improve the commercial viability of the business.

Quantitative assessment

The assumptions were discussed and agreed with the Authority. They represent one way of revising the business model and are not considered exhaustive. We recognise that the suggested reforms will be challenging and will require strong direction and commitment as well as careful financial, legal and operational planning by the Authority.

We have modelled three different variations of this scenario. Firstly it has been assumed that the terms of the service charge and the Authority's interpretation of them remain unchanged and thus the proportion of costs recovered from the tenants remains constant and only the rents increase. This limited reform gives a positive NPV of £8.5m.

Limiting reform to rents only results in the lowest NPV of the three variations and thus this scenario is more vulnerable to falling revenues or costs rising.

Under the second variation modelled, it is assumed that the service charge calculation is revised on renewal of the leases in 2010 so that the Authority no longer covers the vacant areas and the costs to be recovered are divided between the tenants. However, the costs continue to be recovered in line with the current recoverability and the tenants will continue to benefit from the economies of scale resulting from the Authority's bulk purchasing power in the areas of electricity / power, water and waste collection. With a target occupancy rate of 98%, it is assumed that a critical mass of tenants exist to cover the costs without becoming an onerous burden. This gives a positive NPV of £17.8m.

The third variation of the reform scenario assumes that the terms of the service charge are renegotiated so that 100% of all relevant revenue and capital costs are recovered from the tenants. Administration costs continue to be recovered as per the current Authority / tenant split. The calculation of the charge is also reformed so that the Authority covers the charges falling to the vacant trading units only. This variation gives a positive NPV of £26.2m.

All these variations give a positive NPV and it can be seen that the more far-reaching the reforms, the greater the potential return (in NPV terms).

As a sensitivity, we have modelled the same three positions but assuming rents of £8 per square foot (£7 per square foot for the Railway Arches) from 1 April 2010. All variations still gives a positive NPV but £4.8m lower, i.e. NPVs of £3.7m (reform of rents only), £13.1m (reform of rents and some service charge reform) and £21.5 m (reform of rents and 100% recoverability of relevant income and expenditure streams.

Although a higher rental tone may be set for new lettings, it is unlikely that rents will be materially increased before 2010. An opportunity to do so with the renewal of a number of unprotected tenancies expiring in April 2005 was not pursued by the Authority. Therefore, it will need to use some or all of the estimated £4.5 million funds held on the Market Account to finance the capital expenditure programme before 2010. Following the increase to rents, the business should be able to self-finance the planned repair and maintenance programme. It would not be appropriate to delay implementing the programme until the rent increases take effect in 2010 because it may be difficult to attract new tenants and achieve target occupancy rates as well as difficult to justify higher rents to incumbent tenants.

It is recognised that the higher rents may be opposed by the tenants. An increase to £10 per square foot

known overheads have been paid.

represents a 51% increase on the 2009-10 average rent but it is our understanding[18] that there should be no legal impediment preventing rent increases if at the time of lease renewal, rents are set at the prevailing open market rate. However, if faced with a legal challenge, the increase will be more easily justified if the Authority has set a higher rent tone prior to 2010. The ability of existing tenants to absorb higher rents will vary and the Authority may need to consider phased rent increases or regular rent reviews rather than a step change. Nevertheless, it is likely that not all existing tenants will be able to pay higher rents and reform may accelerate their exit from the Market and the Market's move towards higher value-add tenants. Additional work would be needed to assess the impact of higher rents on current occupants and on attracting new tenants.

It is also noted that existing tenants may challenge changes to the terms of the service charges under Landlord and Tenant Legislation, thereby delaying reform. However, further delays to reforming the business may jeopardise the future viability of the Market as its physical decline continues and the political appetite to support a confrontational tenant community diminishes. The level of support or opposition from the tenants will heavily influence the deliverability of the reforms and the sustainability of the business.

In order to minimise the risk of challenge by the tenants, the Authority will need to demonstrate that current rents are below open market rates and that current rents and service charges are not sufficient to cover the operating costs of the market or the capital renewal of the market facilities. It would also be important to clearly present how the new regime would be beneficial to all stakeholders.

The projected cash flows of the business under this scenario do not take into account the possible cost of reconfiguring the site or the potential sale of surplus land. These are discussed under scenario 4 below.

Qualitative assessment

Reforming the market business will provide the best opportunity for meeting not only Defra's objective to maintain a viable market but also the similar objectives of the Authority, tenants and local councils.

The Market is viewed positively within the local area, and enhances the social environment by providing employment and supplying produce to local businesses. Consequently, developments within the Market will serve to maintain, if not improve, employment prospects within the locality, and will be supported by the local borough councils.

The Market helps to reduce road traffic in Central London by acting as a central distribution hub which already allows some consolidation of supplies. This would increase with the development of a composite market. Given the Market's operating hours, deliveries can be made at largely off-peak times, thereby reducing peak-hour congestion and associated pollution levels.

Improvement of the site and infrastructure will also improve the internal Market environment. Positive reactions have been received from a number of tenants who feel that they would benefit from improved facilities. In addition, better infrastructure should enable market traders to better react to changes in the external markets, enabling them to remain competitive as the industries develop.

However, a number of tenants have expressed concern about increases in rents and service charges that will be necessary to refresh and maintain the Market facilities. The varying financial positions of the tenants inevitably means that some are better placed to absorb increased costs whilst others believe that they will cease to trade in such circumstances. This could have a negative impact on employment, although it is likely that businesses will be replaced and so the net effect on employment may be limited.

The flower traders are likely to experience the greatest financial difficulties resulting from an increase in rents and service charges. Due to industry trends and new entrants, many have suffered from a

[18] Based on comments made by King Sturge and Pinsent Masons at the PwC workshop held on the 5th September 2005 for Defra and its advisors.

reduction in custom, and have increasingly lower profit margins.

There is no immediate need for legislative change to reform the Market in the manner envisaged in this scenario. However, activities are currently constrained by the 6 2/3 mile rule and the legal challenge by the Corporation of London over face-to-face fish and meat trading.

The success of any reform is dependent on the cooperation of the tenant community. There is a risk that changes are contested legally or relations between the Authority and tenants sour to such a degree that all changes are opposed, blocked or delayed.

Conclusions

Reform could be undertaken by the Authority with its new Chairman and Board currently acting as catalysts for change, although it is too early to comment on the substance and effect of their actions.

Changing both the rents and service charges would help to create a sustainable business. However, such increases will inevitably impact upon the market tenants and their ability to continue trading. If businesses fail, it could lead to opposition to further changes. At this stage, there is insufficient information to understand the likely impact of such changes on the tenants. Notwithstanding this, without some form of change, the financial sustainability and existence of the market could be threatened.

Reforming the business may increase the disposal value of the site as a buyer would be buying not only the site but also a profitable business. Turnaround of the business would have to wait until 2010 when the majority of lease agreements are due for renewal, although the procedures necessary for reform would have to be in place much earlier. Reform would help maintain the market as a commercially and financially sustainable business which would help assure its long-term existence. The deliverability of this scenario is heavily dependent on the necessary will from within the Authority to start a robust reform process as soon as possible and on the support of a range of stakeholders.

6. Scenario 3 – Closure

Overview

This scenario considers the costs and risks associated with closing the Market and selling the site for redevelopment. This assessment of the quantitative and qualitative aspects of closure provides an additional baseline for comparison with the other scenarios.

The analysis below considers the appropriate timing for closure, considering the current lease agreements, and the restrictions placed on landlords by the Landlord and Tenants Acts. For the purposes of this scenario, the optimal closure year is 2010, to coincide with the expiry of the majority of the tenant leases. The small number of leases expiring in 2015 would be bought out, assuming that the additional costs are preferable to delaying disposal for a further 5 years.

It is assumed that the Authority would continue to own the Market until redevelopment was possible. Quicker disengagement (as soon as legislation allowed) would probably involve the transfer of the site together with the incumbent tenants and the business would continue under the auspices of a different organisation. Defra may be able to secure general assurances over the continuation of the market but it is likely that the new owner would allow the business to decline in order to realise the development value of the site. As the new owner would be liable for the closure costs, master planning and obtaining planning permission, Defra would expect to receive a heavily discounted price for the site to take account of the uncertainties and risks.

If the Market is extinguished, we understand that the local planning authorities would probably oppose redevelopment of the site until convinced that there is no future opportunity for the market to return.[19] Therefore it is estimated that the site would have to be marketed for its current use for a period and demonstrated that no alternative operators exist, before an application for redevelopment could be considered. It is assumed that the planning authorities will seek to restrict future uses of the site to business / industrial / warehousing uses. However, the length of the marketing exercise and inability to find alternative market operator may influence the potential for approval of alternative uses as the planning authorities would not want to see the site vacant for an extended period.

Future development of the site will have to be in accordance with the London Borough of Wandsworth (LBW) Unitary Development Plan (UDP) and the London Plan. The latter identifies Vauxhall/Nine Elms/Battersea as an Opportunity Area. This area is allocated to accommodate 7,500 new jobs by 2016. Nine Elms is identified as a key node for London's wholesale markets. The Nine Elms / Queenstown Road Industrial Employment Areas (IEAs) have also been identified as a Strategic Employment Location (SEL), which the Mayor intends to promote and manage so as to retain a strategic reserve of industrial capacity.

The UDP recognises that there has been a gradual decline in trade at the New Covent Garden Market. Paragraph 208 of the UDP notes that the LBW "supports the continuation of the market at Nine Elms together with improved utilisation of this major site in order to generate further employment opportunities

[19] Based on discussions with Drivers Jonas and King Sturge.

for appropriate business uses associated in particular with Central London activities, exploiting its locational attractions and available land and premises. The market area could for example increasingly focus on new enterprises involved in food preparation and catering services and other specialist business activities. It is also clear from the UDP that LBW will continue to support the expansion, conversion or redevelopment of sites or premises for business (B1), industry (B2), and/or warehousing (B8)[20]. .

In the event of total closure and redevelopment, the LBW would need to refer to Section 54A of the Town and Country Planning Act 1990 (as amended) and Section 38(6) of the Planning and Compulsory Purchase Act 2004, in considering any redevelopment scenarios. These require that applications for development accord with the provisions of the Development Plan, unless material considerations indicate otherwise.

It would be possible to enter into discussions with LBW to seek to persuade them to revise the Development Plan, so as to permit a degree of residential or mixed use development. This would, however, take some time. The prospect of agreeing any changes would depend in part on the proportion of the site which it was intended to use for other than business / industrial / warehousing purposes, and hence the employment implications of any change in use.

For the purpose of the closure scenario – where the whole site would be affected – we have conservatively assumed that planning permission would be restricted to business / industrial / warehousing uses. However, it is possible that, if the site was left unused for a significant period and evidence of a lack of demand was presented, the planning authority could adopt a more flexible approach.

The following key assumptions have been made:

- The activities of the market would continue as per the current business model until the 31st March 2010 when the majority of leases expire.

- Rents and service charge recovery would remain at current levels.

- Once closure was announced or inferred, current activity levels may be affected. However, it is assumed that the tenants would stay until 2010 to fulfil their ongoing legal commitments under their leases. By staying, they would continue to benefit from below market rents and would be eligible to apply to the courts for compensation under the terms of the Landlord and Tenants Legislation when the leases are not renewed.

- For the purposes of the cash flow analysis under this scenario, it has been assumed that the fruit and vegetable and flower markets close and no alternative site is offered to tenants.

- On closure, it is probable that the analysis would face considerable closure costs. In particular, compensation could be payable for not granting new leases and lost income as well as the expected legal costs to negotiate a settlement with the tenants. The level of compensation will be determined by the length of the Tenant's interest in the property. If it exceeds 14 years, they will be entitled to two times their rateable value. Any interest less than 14 years will be calculated at one times rateable value. For the purpose of our calculations, we have assumed that all tenants have an interest exceeding 14 years. The pension short fall and redundancy payments could amount to £2.5-£3 million with total closure costs of approximately £10m being estimated. There will be significant cash flow implications in the years when these amounts become payable. Lost income compensation costs are not currently included as there is insufficient data to support what could be substantial costs (estimates based on experience and "gut-feeling" range from £10 million to £15 million).

- As noted above, it is assumed that the planning and other authorities restrict the immediate

[20] Policy BIN 2 of the LBW Unitary Development Plan.

redevelopment of the site for alternative uses. In order to meet the requirements of the LBW UDP and the London Plan, alternative uses of the site will have to be put forward as part of a comprehensive scheme. We estimate that a possible redevelopment programme may take up to 4 to 5 years from market research to planning permission. It is assumed that this process commences around the time of closure as the period between the announcement and actual closure is used to test whether alternative operators exist. An announcement to close the Market is likely to provoke opposition among key stakeholders and this may delay the approval of any redevelopment programme by the planning authorities. Therefore we have assumed that disposal takes place 5 years after closure in 2014-2015. A variation has also been modelled, assuming that the process of assessing alternative operators and gaining planning permission is completed satisfactorily much earlier and the site is sold in the year after closure, i.e. in 2010-11. This would imply a very early decision by Government on closure.

- According to a copy of lease SGL 73044 provided by the Authority, J. Sainsbury Ltd has a right of access across the site regardless of whether the markets are operational[21]. Therefore, the site will remain open during the intervening period between closure and disposal and it is assumed that the Authority will continue to generate revenues from the non-core sites, such as the Sunday Market, general coach and care parking, Esso petrol filling station, as well as from Royal Mail, BMW and Banhams.

- Whilst occupancy of the Railway Arches will drop sharply immediately after closure of Markets, it is assumed that new unrelated tenants will be prepared to rent the space.

- Certain running costs will be incurred for security, cleaning and waster disposal, utilities and administration.

- It has been assumed that the whole 56 acre site will be sold for light industrial use, consistent with the UDP. Current estimates indicate that Defra could expect to obtain £1 million per acre. This value does not take into account any potential premium for a site of this size, the possibility of a broader range of uses, or the potential liability for dismantling costs or site clean-up costs.

Quantitative assessment

Based on the operational and revenue / cost assumptions discussed above and in more detail in Appendix A, the closure scenario generates an estimated free cash inflow net present value of £22.4 million. Under the second variation where market research, masterplanning and other planning processes are completed within a shorter timeframe, disposal takes place in the year after closure and generates an estimated free cash inflow net present value of £33 million.

These figures are highly sensitive to the assumed disposal date, the planning permissions granted (and hence the value of the site) as well as the closure costs incurred. The assumed value of the site will only be realised if appropriate planning permission can be obtained to redevelop the site. Significantly greater values could be reached if different planning permissions (e.g. including an element of mixed use and / or residential development) were assumed. Even if planning permission is granted, there will be a holding period during which time the land cannot be redeveloped. Throughout this period the Authority would continue to incur costs, such as security and utilities.

As noted above, a quicker disposal with the closure of the markets falling to the purchaser could result in a lower disposal value heavily discounted for uncertain closure and planning costs and risks.

As noted above, this figure does not take into account the state of the site at disposal. Costs of

[21] "A right of way with or without vehicles between the hours of 7.30am and 7.30pm every day other than on Sunday [...] (a) over and along such of the roads within the [...] Market and in particular (but without prejudice to the generality of the foregoing) (b) over and along the road shown coloured brown on the plan to the point marked "D" to the extent needed to provide reasonable access for commercial vehicles delivering goods to the property and the buildings" (Para. 9.2 (a) and (b) SGL 73044).

dismantling the market fabric and clean-up costs have not been estimated. If Defra decides to close the Market, additional factors to consider include the cost of extinguishment of business compensation under the terms of the Landlord and Tenants Legislation and whether compulsory purchase of leases is possible and / or desirable. This figure also makes no allowance for the substantial lost income compensation costs of potentially £10m plus in 2010.

Qualitative assessment

There are significant legal issues which will need to be overcome if the Market is to be closed. The Covent Garden Market Act 1961 stipulates that the Authority has a statutory duty to provide market facilities. Such legislation will need to be repealed before the closure can take place. Closure of the Market is likely to meet significant political resistance, due to the impact on the tenants, the employees and the local community. (Hybrid) legislation giving Defra the legislative power to disengage could be blocked if closure of the market is opposed.

The tenants may challenge the Authority's refusal to renew the leases expiring in 2010. As the Authority could be unable to demonstrate or satisfy the terms of Section 30 (a) to (g) of the Landlord and Tenant Act 1954 (i.e. unable to demonstrate development because of a lack of planning permission), tenants may be granted relief by the courts. This could mean that the courts will grant new leases to the tenants. Therefore, compulsory purchase will need to be considered. However, given the demographic profile of the directors of the tenants businesses, it is possible that a large number will seek extinguishment compensation (i.e. the Authority would have to purchase their business). This generally leads to a higher compensation claim or consideration for the scheme, higher publicity for the action and certainly a higher degree of political discomfort.

Further work would be required to determine whether the Authority has the powers to undertake such compulsory purchases, and the extent to which this would be opposed politically.

The tenant community will be substantially affected by the closure of the Market. A number of businesses have suggested that they would be unable to absorb commercial rents elsewhere in London. Others are concerned that they would lose their local client base, especially if forced to relocate outside of Central London.

Whilst some tenants believe that they would relocate elsewhere, tenants think it unlikely that all the traders would relocate to the same place, effectively creating a new market. As a result, wholesalers will lose much of their trade from on-site catering distributors, and the distributors will lose the competitive advantage in terms of choice and convenience by being located so close to the wholesalers. On closure of the Market, it is likely that customers would source their supplies from the Spitalfields or Western International markets.

The impact on the local external environment will be dependent on how the land is redeveloped. In the short term in the period between Market closure and land sale, there will be a significant impact on employment. It is estimated that approximately 2,600 people are employed by market-based businesses.

Conclusions

While unacceptable to a number of stakeholders, closure may become the default option if no action is taken or reform of the business fails. This scenario would meet Defra's objective of complete disengagement and it could be achieved within the desired timeframe (i.e. by 2008) if legislation is passed and Defra is willing to accept a heavily discounted price.

Whilst the NPV of this scenario looks potentially attractive, the forecast closure and compensation costs are estimates only and may be incomplete. The NPV is also very sensitive to changes in the disposal value of the site and the timing of the sale.

This scenario does not meet Defra's publicly stated other objective of providing for the continuance of a financially and commercially viable market.

7. Scenario 4 – Reform & Redevelopment

Overview

The reform and redevelopment scenario follows on from scenario 2 and examines the potential for reforming the business and redeveloping part of the site. The key business reforms are setting open market rents at the earliest opportunity, redrafting the terms of the service charge agreement to recover a higher proportion of Market costs (revenue and capital expenditure) and revising the service charge calculation so that the Authority covers the charges falling only to the vacant trading units.

The site comprises some 56 acres of land. The site is essentially in three parts (see site plan at Appendix E).

- Part A is the flower market which is on the north side of the railway line and is approximately 5 acres in area. This part of the site is close to the river and is less than a five minute walk from the transportation hub of Vauxhall. A number of other nearby sites have been developed into tower blocks of high quality apartment style accommodation with some river views.

- Part B is the main part of the site covering approximately 46 acres south of the railway line and houses the fruit and vegetable market. It has road access via a tunnel from the north under the railway line. The boundaries for this part of the site are the railway line, social housing and a supermarket.

- Part C is the entrance to the site north of the railway line but separate from Part A by light industrial units (current occupants include the Post Office and logistics firm DHL) and covers approximately 5 acres. Part of this site has been sub-let for light industrial uses (e.g. parking for the Post Office) while part remains vacant. The main entrance to the site is from the Wandsworth Road.

In considering the redevelopment scenarios we have taken into account the views expressed through the interviews undertaken with the Authority, Defra, Nicholas Saphir, Wandsworth Council and other stakeholders and interested parties. There is a consistent proposition which emerges from these discussions and which centres on the disposal of the current flower market (Part A) and relocating those tenants to a new purpose-built building on the main part of the site (Part B).

At this stage, we have considered one existing design / example for site reconfiguration informed by the work undertaken by GMW under instruction from the Authority. A full master planning exercise undertaken either by Defra with the support of the Authority or by a third party purchaser could propose more appropriate or innovative designs. The core elements of the GMW design are:

- Part A could be redeveloped, subject to planning approval, for new residential accommodation with the potential for an apartment style tower block. Some affordable housing will be necessary on the lower floors to secure planning permission for the whole scheme.

- Part B could be reconfigured so that a flower market is constructed on the site of the current Pavilion and more generally the wholesale and catering facilities of the fruit and vegetable markets are updated / reconfigured.

- Part C could be used if necessary for decant purposes in the short term and then redeveloped for affordable housing as a means to obtaining planning permission for the luxury residential development on Part A.

While it is recognised that the above is a highly specific example, the Authority considers that it would need some significant further development in order to meet the practical needs of a 21st Century market. It is also recognised that before proceeding with any form of redevelopment, there would need to be a robust business case for continuing to provide flower market facilities at Nine Elms. Nevertheless, it helps to illustrate that some form of site reconfiguration and redevelopment could generate substantially better value compared to the previous scenarios. It also provides a starting point for discussion and further debate.

To estimate the net present value of the free cash flow generated by this scenario, the following key assumptions have been made:

- It is assumed that rents are increased to open market rates from the 1st April 2010 for leases being renewed. Occupancy levels of trading units increase from 2007-08 and these new lettings are let at open market rents. These business reform assumptions are detailed at scenario 2 above and Appendix A.

- The terms of the service charge agreement are redrafted so that 100% of all relevant costs are recovered from the tenants. The service charge calculation is revised so that void offices are excluded and the Authority covers only the charges falling to vacant trading units.

- It is assumed that it takes 3 years to obtain the necessary planning approvals for the above redevelopment proposals. It is estimated that planning fees of £700k will be incurred.

- Vacant possession of the Pavilion is achieved by mid 2009-10 for its demolition. There are approximately 15 tenants in the Pavilion and it is assumed that the Authority is able to negotiate their relocation to other trading units. Negotiation is preferable and more practical than serving compulsory purchase notices.

- It is assumed that construction of the new flower market facilities will take approximately 2 years and cost an estimated £5.3 million[22].

- Vacant possession of the old flower market is achieved by not renewing the leases expiring in 2010. It is assumed that the Authority is able to satisfy the courts that the leases protected by the security of tenure provisions of the LTA 1954 should not be renewed on the grounds of the landlord's intention to redevelop the site. Therefore, it is also assumed that the necessary planning permission has been obtained and that there is a contract and funding agreed for the redevelopment.

- It is assumed that the disposal value of Part A amounts to approximately £10 million[23] per acre and therefore £50 million in total for the 5 acre site. The sale of Part C for affordable housing is linked to the disposal of Part A and it is assumed that the developer has taken it into account when agreeing the purchase price.

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[22] Source: RICS/BCIS and PwC

[23] Source: PwC estimate based on VOA historical data

Quantitative assessment

The assumptions for reforming the business were discussed and agreed with the Authority. As noted above, these reforms are illustrative and other approaches may be more effective.

Based on the above operational and redevelopment assumptions above and in the more detail in Appendix A, this scenario generates an estimated net present value of approximately £50 million. This figure is sensitive to the level of business reform achieved, the assumed value of the site, and the cost of reconfiguring the site.

As under the reform scenario, we have also modelled the NPV assuming rents of £8 per square foot (£7 per square foot for the Railway Arches) from 1 April 2010. This variation gives an estimated positive NPV of £45.5m, i.e. £4.5m lower.

Qualitative assessment

A commercial lease will benefit from automatic rights of renewal on its expiry as governed by the Landlord and Tenant Act 1954 unless both the landlord and tenant have specifically agreed to omit these rights via the Courts prior to lease commencement. It is likely that all flower market tenants will have specifically applied to the courts to protect their leases. However, even though these rights exist to protect the Tenant's occupation of the premises in the future, there are certain grounds that allow a landlord to object to a tenant's request to a lease renewal. These are set out in s.30 (1) of the Act:

a) Failure to comply with repairing obligations

b) Persistent late payment of rent

c) Other substantial breach of lease terms i.e. illegal subletting/assignment/alterations

d) Landlord can provide a suitable alternative property

e) Uneconomical sub division

f) The Landlord intends to redevelop

g) The Landlord intends to occupy.

It is very unusual to rely on part (d) providing suitable alternative accommodation as grounds for not renewing a lease. We understand that in practice tenants easily find reasons why the new accommodation is not suitable[24]. Moreover, the Authority would wish to charge higher rents and service charges for the new premises in line with its reformed business model and so it would be difficult to satisfy the courts that it was suitable alternative accommodation.

Therefore, an easier route would be to prove redevelopment of the site. However, it must be stressed that in order to satisfy the courts that this is a valid ground, the landlord must show a firm intention to redevelop (Case: Cunliffe v Goodman), e.g. by having the finance in place, and demonstrate that possession of the site is necessary to undertake the work.

If the courts are satisfied that the redevelopment grounds apply, a tenant will lose their automatic lease renewal right although they may be able to claim compensation. The level of compensation is determined by the length of the tenant's interest in the property. If it exceeds 14 years, they will be entitled to two times their rateable value and any interest less than 14 years will be calculated at one times rateable value.

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[24] Based on advice from Pinsent Masons at the PwC workshop held on the 5th September 2005 for Defra and its advisors.

In practice, if by 2010 planning consent had been given to redevelop the flower market site but the new accommodation was not completed, the Authority could offer new leases with a break-clause to be exercised with 6 months notice as soon as the building is ready. If planning consent is in any doubt, it will be up to the discretion of the courts to allow such a break-clause.

Any scheme for this entire site would have to be brought forward as part of a comprehensive approach. Discussions with the planning authorities would need to be advanced before any residential use could be considered. Initial discussions with Wandsworth suggest that they are open to the general principle behind redeveloping the Flower Market and Entrance sites but that they would need to see more advanced proposals.

The impact upon the market business during any redevelopment needs consideration. If there is significant disruption or upheaval for customers, this may cause them to look for alternative suppliers. However, careful planning and using Part C as a decant site should help to overcome some of these issues.

The most difficult part of any redevelopment is predicting what the market part of the site should look like for the future. The current market represents best practice from the early 1970s for a wholesale horticultural market whereas today the market operates more as a logistics park and catering distribution centre. The site design is not optimal for this logistics role or indeed for the wider use by catering businesses which now occupy some 70% of the original wholesale site.

In addition to site layout, future requirements for the structure and fabric of the buildings centre on what will make up the Market business in the future. As discussed in the market overview section, there has been a great deal of change over the past 20 years in the operation of wholesale markets particularly given the growth of the supermarkets. This suggests that a comprehensive master planning exercise should be undertaken before any redevelopment.

Before restructuring the fabric of the market buildings through a redevelopment, the market needs to understand where its future lies and indeed what is meant by having a market both today and in the future. If the growth in the catering business looks set to continue with a continuing decline of the wholesale business then a greater emphasis should be put on providing facilities which maximise the potential for the catering business and reduce the space required by the wholesale market. Equally it could be assumed that the flower market will continue to decline and therefore a smaller flower facility could be provided.

The need for flexibility is fundamental, particularly if the market becomes commercially owned after disposal by Defra as it will need to respond to market forces quickly and effectively. Any new building should be designed and constructed to allow for maximum flexibility.

Conclusions

Our analysis has shown that reforming the business and partially redeveloping the site should generate better value. Our analysis is based on a number of assumptions and is highly sensitive to the level of reform and the disposal value of the site.

It is important that redevelopment is linked to reform otherwise the business will be seeking additional support in the future. As for scenario 2, it is important to start the reform process as soon as possible in order to take advantage of the natural break in 2010 when the majority of leases expire.

It is also important to start planning the redevelopment of the site as soon as possible to allow sufficient time for master planning, obtaining planning permission and finding a suitable developer.

This scenario best meets Defra's criteria of disengagement, maintaining a market and deliverability. However, it is unlikely that Defra's preferred timescale will be sufficient to implement the reforms needed or to develop fully the redevelopment options.

8. Disposal options

Consideration now needs to be given to both the timescales and the method for Defra of disposing of its interest in the Market. The options for disposal depend upon a number of competing issues for example the legislation that is currently in place, the drive to maintain a market, the inherent value in the site both in terms of that which is released under any redevelopment scheme and that which remains in the land on which the core market is situated.

In understanding the options Defra has for disposing of the Authority there are two main factors which influence both the timing and route chosen. Firstly, there is the issue of legislation and whether any option can be taken forward prior to legislative change. The second issue is around the business of the Authority. There is a decision point as to whether a disposal takes place before any reforms of the business are implemented.

These two factors also need to be considered within the wider issue of Defra's main assessment criteria for reaching a decision on the route to take forward. These criteria were agreed with Defra as:

- Defra completely disengaging from market ownership;
- disengagement within Defra's desired timeline (2008 or as soon as possible thereafter);
- the provision for continuance of a financially and commercially viable market; and
- a deliverable solution (given the diverse range of stakeholders).

Looking at these criteria it is apparent that those solutions which can be considered without legislative change do not give the complete disengagement Defra requires. Given this, whilst we have outlined below some potential solutions which could be achieved without legislation, these are at this stage included for completeness only. The focus has been placed on options which will require some form of legislative change and thus meet the primary criteria of disengagement. It is our understanding that the earliest point at which such legislation could be achieved is 2007/2008.

As regards the business of the Authority, Defra wishes the continuation of the market in a financially and commercially viable way. To achieve this from the current operating position the market requires a major change in terms of its operations including reorganisation of senior management and instituting long term planning as to the shape of the business going forward. This has been discussed in detail in sections 3 to 7. This change is likely to take a couple of years although the change process is already under way. There is also the constraining factor that any major changes to the way in which the market is organised will only be able to be implemented when many of the current leases can be re-negotiated for commencement in 2010. Prior to this point, whilst some small changes can be made, changes to the levels of rents and service charges are likely to be limited.

The possibility of major structural changes in the ownership of the market before such reorganisation is completed could well cause uncertainty, resulting in decline and thus impact on the possibility of sustaining a financially and commercially viable Market. Such uncertainty in the past ten years has been one of the main reasons the Market has stagnated; and it is critical at this juncture that a clear plan is given to the market traders and all other stakeholders to give them the belief that the market business will continue if a viable Market is to be created.

We have set out below the options for Defra's disengagement from the Authority. These are:

1. Rapid disposal option (as soon as legislation allows)
2. Improved value disposal option
3. Transfers within the Public Sector
4. Pre legislation options

Rapid disposal option

Description

Assuming that Defra was in a position to achieve hybrid legislative change by 2007/8, this is the first opportunity for a complete disengagement from its responsibilities for the Authority. As discussed below all other options prior to this point would rely on some form of long lease structure which would still leave the freehold interest in the land with Authority. This in turn would require Defra to keep in place the necessary administrative machinery set out in the current legislation to support the Authority, which it is our understanding does not meet with Defra's prime objective of divesting itself of all non-core activities.

Given this, the earliest point at which Defra could look to sell the site with the incumbent tenant of the market business would be in 2007/8. This would require commencement of a sale process up to 18 months before the sale of the site, meaning Defra would need to start such a process within the next 12 months to achieve the earliest sale.

A development competition would be run to select the purchaser. The evaluation of offers would be based upon the price offered for the site both in terms of day one value generated and claw back offered. Claw back is often used in the sale of development sites to allow the seller to obtain a share of any future profits. This can impact on the price offered at the point of sale as the upside to the developer is limited by claw back. Some claw back arrangements are time bounded and this can lead to developers delaying sales to avoid paying out claw back. A sale and purchase agreement would then be entered into by Defra, the Authority and the purchaser which would need to include covenants to ensure the continuation of the Market on the site.

Under this option the site would be offered without any form of planning permission as there would not be enough time prior to commencement of the sale process to gain such permission and it would be for the purchasers to progress such discussions with the planning authorities both in terms of initial master planning and detailed planning and take the risk on any value uplift achieved through such planning.

Comments

From Defra's perspective one of the key criteria for assessing potential options is the deliverability and thus potential success of implementing a proposal. Under this option the sale process would go ahead prior to the reorganisation of the market business being completed which could lead to uncertainty as to the future of the Market. Such uncertainty could lead to political opposition and thus delay the passage of hybrid legislation. Equally the impact of the uncertainty on the Market could affect its long term financial and commercial viability.

Any potential purchaser approaching such a transaction will analyse the potential for the site based upon the lack of planning permission and the covenant of the incumbent tenant. They will apply a risk factor for these issues which would reduce the amount offered for the site and will also discount the value offered for the time period they assess it will take to achieve planning permission.

The evaluation of such bids will be difficult as they will be based on different assumptions regarding planning and likely timescales and thus it could be difficult to determine which bid offered the best financial solution to Defra. Equally, once a purchaser had been chosen there may be some difficulty in negotiating the necessary covenants required for continuation of the Market on the site. This will be complicated by the fact that change to the Market is restricted until 2010 due to the existing lease agreements and the determination of what is needed to support the market in terms of both space and logistics will be at best unclear. Such issues will impact heavily on the price offered for the site and the sale and purchase contract.

Post sale the purchaser will then be in a position to gain a potential windfall by obtaining an enhanced financial position from that which their purchase price was based on through negotiations with the planning authority. Whilst an element of this could be recovered through a claw back provision, such clauses can be difficult to enforce particularly if they are time limited.

Under this approach it is difficult to see that Defra would be gaining best value for money due to the discount applied by the purchaser. Indeed experience from other governmental organisations suggests that the approach of selling a potentially valuable site prior to gaining planning permission is no longer considered to be best value for money. For example, British Waterways Board told us that they no longer follow this approach, preferring to gain strategic planning permission for sites or enter into long term partnerships to ensure they gain best value from sites. The Ministry of Defence is also moving away from any approach which does not allow it to fully share in any value uplift, preferring long term partnering approaches to achieve this.

This disposal option would be open to challenge by the NAO and others within government as not providing the best result for the taxpayer.

Improved value disposal option

This option allows for complete disengagement for Defra from the Authority by 2010. There are three main strands to this approach; turnaround of the business, master planning and site strategy; and hybrid legislation.

As discussed in section 5 the Board of the Authority has changed in the last few months and the process of reorganisation of the senior management has commenced. However, it is likely to take some time for the impact of this to show through and the real time at which demonstration of turnaround of the business can be shown will be at the break point for most leases in 2010. Until this point, whilst some changes can be made with new leases potentially being negotiated on improved terms any changes will be limited. Over the next year to two years Defra will also need to look at the best shape for the market going forward, considering the level of wholesale markets required on site and the mix of other market activities which may be considered. A key issue here will be to determine how far, as a matter of public policy, an opportunity should be preserved for the non-traditional wholesale activities (e.g. food processing and preparation for the catering trade) to continue on the site, and how far this opportunity should be restricted to more traditional activities. This strategic view will then inform the site requirements for the market, in particular the logistics needed to support the business, the land required and the layout of any new market buildings.

This strategic vision for the future of the Market can then feed into the master planning process. Under this option Defra and Authority would undertake master planning with a view to agreeing a development brief with Wandsworth Council. Gaining such a brief would enhance the site's value and yet still give potential individual purchasers the opportunity to develop detailed plans, thus giving room for innovation. Defra would engage master planners to carry out this process working closely with the Authority as to the requirements for the Market in the future. In this way the greatest value for the site would be generated whilst giving the best opportunity to the Authority to create a financial sustainable market. Working together with the Market in this way will also maximise the employment opportunities which is likely to help in achieving the optimum planning permission for the site.

Although 2010 would be the obvious implementation date, as it coincides with the new lease terms, Defra could consider implementing this approach sooner, if the master planning exercise had been completed and the legislation passed this would be done on the basis that the reforms of the Market business had been planned and prepared, albeit that they would not be implemented until 2010.

The final strand in this option, working with the master planning and reorganisation of the business, is the progression of hybrid legislation. The strategic vision for the Market together with the master planning will mean that the legislation is likely to be widely supported by stakeholders given the additional security it

The investor would have an obligation to make part of the site available for "market business" and would be the Landlord to the market tenants, charging rents and providing property services, in return for a service payment. The investor would undertake redevelopment and take the benefits of the redevelopment, subject to its obligations regarding the market business. The head lease would include covenants and obligations regarding the continuity of the market business on site and would include claw backs for property gains/developments.

The timescale for this option could be around 12-18 months, but may take longer.

Comments

The value realised would be based on the current market rents and the long term un-sustainability of the current market business which could result in a low value being achieved for the grant of the Head lease i.e. this is effectively Defra disposing of a problem not a business

Whilst there would be legal restrictions protecting the market, the commercial incentive of the Property Investor would not be aligned with this, as the investment return from the market is less than could be achieved through other activities e.g. development of the site for residential use.

As with any rapid disposal undertaken without master planning and discussions with the planning authority, there is the potential of a windfall gain for the Property Investor which could lead to criticism of Defra.

This option would also be subject to confirmation that it was consistent with the Authority's statutory duties.

Medium term contracting solution - Management contract 5 year plan

The Authority would enter into a 5 year management contract, outsourcing all the facilities management services and also the collection of the rents to a Contractor which could potentially include transferring the revenue risk of collection of the rents to the Contractor. The Contractor would be chosen through an open competitive process to ensure transparency and best value. Authority would retain the named personnel required under the legislation but with responsibilities limited to dealings with the Contractor and carrying out the required capital works.

The timescale for this option would be a total of 18 months with 12 months required to undertake a review and reconfiguration of the Market Authority business and 6 months for the open competition and granting the management contract.

Comments

This option offers the potential for lowering the management costs of the Authority and improving performance through an open competitive process. The Contractor would be incentivised to attain higher recovery of direct costs through the service charges.

This is only a short to medium term solution as it does not deal with the wider property issues or permit Defra to fully disengage from the Market. It could, however, be put in place whilst the wider redevelopment issues and legislative issues are considered leaving both Defra and the Authority some medium term flexibility. It is essentially an alternative to achieving reform of the business by strengthening the management.

Long term contracting solution – long term (25 year) management contract

The Authority would enter into a 20 to 25 year contract which would include all the facilities management services, collection of rents, as well as the required capital works. This could potentially include transferring the revenue risk of collection the rents to the Contractor. The Contractor would be chosen through an open competitive process to ensure transparency and best value.

In essence this could be seen as the 'operational' phase of a PFI contract with some lifecycle responsibilities for the property. Under this option Defra would again retain the site to rationalise and redevelop.

The timescale for this option would be a total of 2 years with 12 months required to undertake a review and reconfiguration of the Market Authority business and 12 months for the open competition and granting the contract.

Comments

There would be a significant interface between the site rationalisation and management contract which could impact on the rationalisation opportunities and negatively impact value for money

This option offers a potential long term (but not permanent) solution, although the contract could be re-let at the end of the concession period.

Long term partnering solution – Contract to redevelop site with sharing of benefits plus 25 year management contract

The Authority would enter into a 20 to 25 year contract or joint venture which would include all the facilities management services, collection of rents, as well as the required capital works. This could potentially include transferring the revenue risk of rent collection to the contractor.

The Authority would also enter into a partnership agreement or joint venture to redevelop the site. The proceeds from the redevelopment would be shared with the contractor on a gain share basis. The contractor would be chosen through an open competitive process to ensure transparency and best value.

The process for choosing the contractor would include competing both for the best site strategy for the market and the gain shares for redevelopment and the running of the Authority business over a 25 year period.

The timescale for this option would be a total of at least 3 with 18 months required to undertake a review and reconfiguration of the Market Authority business and 18 months for the open competition and granting the contract.

Comments

This is a compromise option which gives greater certainty over the long term future of the market through a contractual route and allows realisation of benefits from redevelopment without Defra/Authority undertaking this.

It offers a long term but not permanent solution, although the site and business could be sold on to the Partner at the end of the concession.

Gain shares on the redevelopment would incentivise the Contractor to develop the site in the most beneficial way whilst ensuring Defra receives an appropriate return. However, this is a fairly complex solution which would take longer to implement, than a simpler long term management contract.

9. Disposal Methodologies and Mechanics

Introduction

Irrespective of which of the four disposal approaches analysed in Sections 4 to 7 is adopted, questions will arise as to the most appropriate disposal methodology and mechanics. This section discusses these issues at a high level. A more detailed analysis will be required as part of Stage 2 of the advisory assignment, once Defra has given a steer on the way forward. The analysis in this section assumes a complete disposal of Authority (and hence the passage of the necessary legislation) rather than the less radical options which are reviewed briefly in Section 8.

What is being disposed of?

Although Authority is a single statutory entity its disposal can be considered under two headings:

- Disposal of the market business i.e. the business of letting and managing leases to market traders and other food related businesses, and providing ancillary services.
- The disposal of the development opportunity on the site.

These represent two distinct commercial opportunities.

One transaction or two?

The next question to consider is whether the two commercial opportunities should be disposed of by means of one transaction, or two separate ones.

Final decisions on this will have to wait until, among other things, the site development opportunity has been further defined through the master planning exercise recommended in Section 8. However, there would in principle be strong reasons for having two separate transactions:

- As a general principle, best value may not be achieved by bundling together the disposal of two commercial opportunities with different (or substantially different) pools of potential investors – as this would limit interest in the transaction to those parties (if any) with an interest in both opportunities. In this particular case, the pool of potential interested parties for the market business (probably, the tenants themselves; and possibly some niche property investors interested in portfolios of light industrial leases) would hardly overlap, if at all, with that for the development opportunity on this site (i.e. property developers). Arranging two separate disposals would not, of course, prevent one party acquiring both the market business and the development opportunity on the site if that was how things worked out; but a priori it seems unlikely that this will happen;
- If there were a single disposal it is likely that the pool of investors interested in the more significant opportunity (i.e. the developers interested in the development opportunity on the site) would predominate, potentially subordinating the interests of the market business. This would not be

conducive to Defra's objective of having the market continue as a going concern.

Structuring the opportunities for disposal

The next issue for consideration is what structural form the two opportunities should take.

As regards the market business, with the abolition of the Authority, there would need to be a replacement entity to let and manage the leases and provide the services to tenants currently provided by Authority. The most obvious option is this should be a corporate entity of some kind, either a company limited by shares (CLS) or a company limited by guarantee (CLG). Further analysis would be required during Stage 2 of the risk profile of the entity before determining the best corporate structure. (For instance, a company limited by guarantees would tend to be more appropriate where the entity had a low risk profile; the risk profile would depend, among other things on the quality of the infrastructure and buildings it was to inherit and the length and robustness of its leasehold portfolio).

Whatever the precise nature of the corporate vehicle it would be granted a long (say 125 year) interest in the relevant part of the site and buildings, subject to using them to run a market business (which would require careful but appropriately flexible definition). It would not be allowed to simply shut down the market and redevelop the part of the site hitherto used by the market for other purposes. That would constitute a breach of the terms of its interest in the site, which would thereupon revert to the Secretary of State.

The site development opportunity would most obviously be structured as a freehold (or a very long leasehold) disposal of the site, subject to:

- The granting of a lease back to the corporate entity running the market business;
- An obligation to carry out whatever building work was required on the site to reconfigure it (to demolish the flower market and re-provide appropriate capacity elsewhere on the site, if that was what the master plan required); and
- To refurbish/replace the market buildings and infrastructure to the extent required.

Disposal method

The conventional method for Government disposal of the market business would be by competitive tender. This could work even if the business were structured as a CLG rather than a CLS. Indeed CLGs have successfully acquired businesses from the Government in the past e.g. the sale of the Transport Research Laboratory to a CLG led by management in 1995.

It has to be recognised, however, that there may be little or no interest in the market business other than from the tenants. If there were only one bidder Defra would need to put in place robust arrangements to ensure that it was able to demonstrate that satisfactory value had been obtained e.g. by requiring the single bidder to meet or exceed a benchmark valuation.

The development opportunity on the site would most naturally be sold by a competitive auction process. This would take place on the basis of:

- A development brief agreed with the planning authorities steering bidders as to which kinds of development would be likely to obtain planning permission and which would not (thus avoiding unrealistic bids, or make it impossible to compare different bids meaningfully);
- A master plan setting out the overall future configuration of the site;
- An obligation on the acquirer to relocate and refurbish/rebuild the market facilities in accordance with the master plan and Defra's requirements.

Disposal methodology in absence of legislation

Section 8 considers a number of less radical options for the future of Authority in the event that it proved impossible, for whatever reason, to obtain the legislation to wind it up. It is worth noting, however, that it appears that something approaching the disposal methodologies described in this section could be implemented in the absence of legislation, though there would be some significant drawbacks.

The scenario envisaged is in one in which Defra intends to implement as far as possible the disposal process set out in Section 8 and the disposal mechanics described in this section but without legislation.

On this scenario:

- Defra would prepare for the disposal in the ways previously described (e.g. master planning the site, reform of the market business);
- Authority would dispose of the site to a developer, subject to an obligation on the part of the acquirer to grant a long lease back to it for the purposes of running the market, and subject also to the reconfiguration and refurbishment/rebuilding obligations;
- Authority would then continue in existence as a statutory body, simply managing the portfolio of leases to the market traders and other market occupants.

The workability of this solution would depend on legal confirmation that it would be intra vires for Authority to carry out such a radial disposal of the site.

A clear advantage of this scenario is that it would take legislation off the critical path. The drawbacks from Defra's point of view would be that:

- The disposal would have to be led by Authority, and the strategy would therefore require their agreement. While this may well be forthcoming, the practical difficulty is that it is hard to conceive of how a thinly resourced entity such as Authority would be able to manage such a major disposal, at any rate without drawing on significant external help and funding;
- Authority would remain in existence, and therefore ultimately continue to be a contingent liability for Defra. However the extent of this liability would be mitigated by reform of the business and by requiring refurbishment/replacement of their assets as part of the development scheme.

10. Expressions of Interest

Appendix E includes a summary of the expression of interest received to date by the Authority or Defra for the Market. Fifteen expressions of interest have been received to date from a wide variety of interested parties, ranging from small unquoted companies, to large PLCs, and including two public sector entities (Corporation of London; English Partnerships). Most parties express an interest in maintaining the market operations, but with land released for commercial developments.

One monetary offer has been made by Comer Group for £40m. All the other expressions of interest are limited to outline ideas for the site only.

These expressions show the level of interest in this potentially valuable site, however at this stage there are no developed proposals. It is important that these potential bidders are kept informed of developments to ensure they maintain interest in any disposal of the site.

11. Appendices

A Authority Projections and Databook

B Financial Model Output Sheet

C List of interviewees

D List of publications

E Expressions of Interest

Appendix A: Authority Projections and Data book

COVENT GARDEN MARKET AUTHORITY PROJECTIONS & DATABOOK

IMPORTANT NOTICE FOR ALL USERS

PricewaterhouseCoopers Model & Assumption Book Disclaimer & Copyright Notice

The Model and Assumption Book were developed by PricewaterhouseCoopers LLP ("PwC") for the Department for Environment, Food and Rural Affairs ("Defra") in connection with PwC's study on the future of New Covent Garden Market (the "Market") on behalf of Defra and its contents are strictly confidential.

The Model has been developed using data and assumptions from a variety of sources. PwC have not sought to establish the reliability of those sources or verified the information so provided, nor has the Model been audited by PwC. Accordingly no representation or warranty of any kind (whether express or implied) is given by PwC as to the internal consistency or accuracy of the Model nor any output from it. Moreover the Model does not absolve any recipient from conducting its own audit in order to verify its functionality and/or performance.

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INTRODUCTION

The operational and financial assumptions have been based on historical and forecast information provided by the Covent Garden Market Authority ("CGMA") as well as the experience and professional judgement of the CGMA management team.

Macroeconomic assumptions have been taken from Treasury. Microeconomic assumptions have been based on industry trends where available or the best estimates of the CGMA.

The model has been created to calculate the NPV of the free cash flow generated by the CGMA in four different scenarios:

Scenario 1 – Status Quo

Scenario 1 forecasts the NPV of the free cash flows generated by the CGMA while operating the wholesale New Covent Garden Market ("the Market") at Nine Elms, near Vauxhall in London, as per its statutory duties in the Covent Garden Market Act 1961. It is assumed that costs and revenues continue at current levels into the future.

We have modelled two positions. The first (1a) assumes that there is limited funding for a comprehensive maintenance programme, while the second (1b) considers the impact of implementing the maintenance programme proposed by King Sturge in March 2005[25].

Scenario 2 – Reform

Scenario 2 forecasts the NPV of the free cash flows generated by the CGMA after introducing a combination of measures to reform the business, i.e. increasing rents, reviewing cost recoverability and implementing the maintenance programme proposed by King Sturge. Reform will take place from 1st April 2010 when the majority of leases are due for renewal.

Three different positions have been modelled. Each assumes that rents are increased to open market rates from 2010.

The first position (2a) assumes that the terms of the service charge cannot be changed when the leases are renewed in 2010 and the CGMA's interpretation of the current terms remains the same. Therefore, the service charge remains the same in real terms and is inflated at the same rate as its component costs.

The second (2b) assumes the service charge calculation is revised on renewal of the leases in 2010. All recoverable costs are re-charged to the tenants and the CGMA does not cover any vacant units. However, the running costs continue to be recovered in line with current recoverability.

The third variation (2c) also assumes that the terms of the service charge are renegotiated for 2010. It assumes that the CGMA recharges 100% of all running and capital expenditure costs directly associated with Market operations. The CGMA covers the charges falling to void trading units only.

Scenario 3 - Closure

Scenario 3 forecasts the NPV of the free cash flows generated until the Market closes. It is assumed that the current CGMA business model, i.e. the status quo, continues until closure. Planning restrictions prevent the immediate sale of the site therefore some additional revenues are generated and costs incurred before the sale. The site's value on disposal assumes that it will be restricted to light industrial uses.

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[25] Planned Preventative Maintenance Programme of New Covent Garden Market, King Sturge, March 2005.

Scenario 4 – Reform and Redevelopment

Scenario 4 assumes that the Market business is reformed as per the third variation (c) of Scenario 2 above. It is assumed that the current flower Market site is redeveloped for new residential accommodation. The Entrance site, including the flats at 33 Battersea Park Road, will be sold for affordable housing. The Pavilion site is redeveloped for the displaced Flower Market tenants. It is assumed that the existing Pavilion tenants are re-located to empty units or the leases are compulsory purchased.

The four Scenarios are described in more detail in the main body of the report. The different assumptions associated with each Scenario are discussed in more detail below.

MODEL STRUCTURE

The Model has been produced in Microsoft Excel XP Professional.

On each worksheet, the following methodology has been used:

- all numbers are in £'000 unless otherwise stated;
- model inputs are denoted by cells shaded yellow;
- formulae are denoted by unshaded cells.

The Model comprises a number of linked worksheets which can be split into three categories:

- model inputs;
- calculation sheets; and
- model outputs.

Model Inputs

All the non-time based assumptions are in the worksheet entitled "Constant Assumptions."

Annual income and expenditure assumptions, including capital expenditure, are in the worksheet "Variable Assumptions."

Additional annual assumptions used in Scenario 2 are in the worksheets "2 – Rents WP" and "2b - Recoverable Costs WP" and "2c - Recoverable Costs WP".

Additional annual assumptions used in Scenario 4 are in the worksheet "4 – Rents WP".

The "Market Area" inputs provide a breakdown of the areas available to let, together with occupancy at March 2005.

The inputs in the "Summary of Rateable Values" worksheet comprise the total 2005 Rateable Values for the units and offices from the 2005 Ratings Listing from the Valuation Office Agency's web site.

The inputs in the "Redundancy Costs" comprise a breakdown of CGMA staff as provided by the CGMA.

The "Rents 1985-2010" worksheet is currently an information sheet showing historical rent trends. The rents data was provided by the CGMA.

Model Calculation Sheets

Worksheet	Purpose
Indices	Calculation of the appropriate indices using the macroeconomic assumptions.
1 – Status Quo	Calculation of the NPV of the free cash flow based on the CGMA's current business model. Variation (**a**) assumes that there is only funding for the CGMA's 3-year capital expenditure programme. **Variation (b)** assumes that the CGMA undertakes the King Sturge maintenance programme thereafter.
2 - Reform	Each variation of Scenario 2 calculates the NPV of the free cash flow assuming that rents are increased and that there will be sufficient funds to undertake the capital expenditure programmes.
2a – Reform (Rents Only)	**2a** assumes that the basis for calculating the service charge cannot be changed. The service charge continues at 2005 prices inflated at the same rate as its component costs.
2b – Reform (Rents+GSC)	**2b** assumes that the service charge terms are revised from 2010. Market running costs are recovered from tenants as per current recoverability percentages but the CGMA does not cover the void units.
2c – Reform (Rents+100% GSC)	**2c** assumes that the service charge terms are revised from 2010. The CGMA recovers 100% of all relevant costs and covers the void trading units only.
3 - Closure	Calculation of the NPV of the free cash flow assuming that the CGMA's current business model will continue until closure. There will be a delay before the site can be sold for light industrial use, during which time, the CGMA will continue to receive rental income on non-market sites and to incur some running costs.
4 – Reform & Redevelopment	Calculation of the NPV of the free cash flow assuming that the Market business is reformed as per Scenario 2, variation (c) above. It is assumed that the Flower Market site is sold for redevelopment and the tenants affected are re-located to a new building built on the current Pavilion site.
Market Area	Calculation of occupancy percentages based on areas available to rent and let figures.

Summary of Rateable Values	Calculation of estimated rates for the let and vacant areas of the Market (for the purpose of calculating compensation on lease termination).
Redundancy Costs	Calculation of the redundancy costs payable on the closure of the site.

Model Output Sheets

The "Results" worksheet summarises the Net Present Values of the free cash under each Scenario:

CONSTANT ASSUMPTIONS

The following assumptions are constant throughout the period under review and can be found on the "Constant Assumptions" worksheet.

Project Timing Assumptions

Timing of Cash Flows

The CGMA monthly management accounts for 2005-06 show that costs and revenues are recognised through out the year. The associated cash flows are also spread through out the year. (Source: CGMA)

Model Period

The Model assumes a 15 year time frame in accordance with the Treasury's Green Book "A Guide to Investment Appraisal." The Model assumes a project start date of 1st April 2005 and a project end date of 31st March 2020. (Discussed and agreed with the CGMA)

Start Date for Escalation

Increases to rent (when applicable) and other revenues are effective from the beginning of each financial year. Increases to staff costs and market running costs also occur at the beginning of each financial year, e.g. the electricity contract is negotiated each year and new prices take effect from 1st April. Therefore, it is assumed that cash flows inflate at the start of the financial year. (Discussed and agreed with the CGMA)

Inflation Assumptions

The following assumptions relate to the inflation rates of different cost and revenue streams.

Wage inflation as increase over RPI

Wage inflation is assumed to be 0.5% above RPI so that wage inflation of 3% is assumed. (Discussed and agreed with the CGMA)

Inflation of electricity and heat as increase over RPI

Certain costs are recovered directly from tenants, in particular metered electricity, heat and metered water. It is noted that the CGMA's heat, light and power costs have increased substantially in the past few years with a 16% increase between financial years 2003-04 and 2004-05 and a further forecast increase of 42% to 2005-06. (Source: CGMA)

According to Table 2.1.1 of the July 2005 Quarterly Review of Energy Prices released by the Department for Trade and Industry ("DTI"), gas prices increased by 7.3% between 2003 – 2004 and then by 15.1% between 2004-05. Electricity prices increased by 6% and 11.5% over the same periods. (Source: DTI)

It is assumed that energy costs will continue to increase at a rate above inflation, although not at recent rates. The Model assumes that energy costs continue to rise at a rate of 5% above RPI going forward in the longer-term. (Discussed and agreed with the CGMA)

Costs of non-metered utilities are recovered via the General Service Charge. (Source: CGMA)

Inflation of water as increase over RPI

According to OFWAT, the industry wide weighted average price increase for the five years from 2005-10 should not exceed 4.2 % per year before inflation. The above inflation price increases were set to enable the water companies to deliver the services required and fund quality and service improvements through a £17 billion capital investment programme. (Source: OFWAT)

It is assumed that water costs increase by 4% above inflation for the five years to 31st March 2010 and

1.5% above inflation thereafter as it is assumed that the need for further capital investment by the water companies will be less. (Source: OFWAT and discussed and agreed with the CGMA)

Costs of non-metered utilities are recovered via the General Service Charge. (Source: CGMA)

Inflation of waste as increase over RPI

The 2005-06 cleaning and waste budget amounts to £2,036k, of which £750k relates to waste disposal costs.

According to the CGMA, waste costs have increased at a rate greater than RPI because of the landfill tax and increasingly limited landfill capacity. Landfill Tax is set to increase by £3 per tonne per year, from a current base of £18 per tonne. Landfill disposal costs are also like to rise faster than RPI. Therefore, it is assumed that waste disposal costs rise at a rate of 5% above RPI going forward in the longer-term. (Discussed and agreed with the CGMA)

It is assumed that the cleaning costs increase by RPI per annum. (Discussed and agreed with the CGMA)

Inflation of General and Group Service Charges as an increase over RPI

The costs that are recovered via the General Service Charge and Group Service Charges (e.g. Flower Market Hall temperature control) inflate at different rates. Therefore, as a best estimate, it is assumed that the service charges inflate at the weighted average of those rates. The weighted average was calculated by expressing each cost attributable to the GSC as a proportion of the total expenditure attributable to the GSC as per the June 2005 management accounts. Therefore, it is assumed that the General and Group Service Charges increase by 1.5% over RPI, i.e. 4% p.a. The relative weighting of each cost is assumed to remain broadly consistent during the period being forecast. (Discussed and agreed with the CGMA)

Inflation of Direct Recoveries as an increase over RPI

Direct Recoveries comprise mainly metered electricity, water and Railway Arches waste which are inflated by 5%, 4% / 1.5% and 5% above RPI respectively – see notes above. As water costs represent only 3% of the total Direct Recoveries, it is assumed that Direct Recoveries inflation is 5% over RPI. (Discussed and agreed with the CGMA)

Inflation of Car Parking Charges

The CGMA reviews its car parking charges every 2-3 years and pegs them to local rates. It is assumed that car parking receipts increase by 2.5% above RPI p.a. reflecting the level of increase that the CGMA would expect over a 3-year period. (Source: CGMA)

Taxation

Corporation Tax

It is assumed that profits will be subject to Corporation Tax of 30%. It is assumed that the annual depreciation charge for the new roof only is equal to the Capital Allowances for tax purposes and therefore tax is calculated on the net surplus after depreciation of the roof. The depreciation charge for the roof amounts to £295k per annum. (Source: CGMA)

The Model includes a simple tax calculation as described above. Carrying losses back or forward for tax relief has not been considered.

VAT

The Planned Preventative Maintenance Programme and the Emergency Repairs costs proposed by King Sturge are stated net of VAT. (Source: King Sturge)

The CGMA is able to reclaim VAT on all input costs therefore the net cost has been included in the Model and it is assumed that, where relevant, all other costs are stated exclusive of VAT. (Source: CGMA)

Professional Fees associated with Emergency Repairs and the Planned Preventative Maintenance Programme

King Sturge completed a report titled "Planned Preventative Maintenance Programme of New Covent Garden Market" for Defra in March 2005. The estimated costs for emergency repairs as well as planned preventative maintenance excluded professional fees and VAT. According to paragraph 1.4 of the report, an allowance of 12% should be added for professional fees. (Source: King Sturge)

Working Capital Assumptions

We assume that debtors take 30 days to pay the CGMA and that the CGMA takes 30 days to pay its invoices. (Source: CGMA)

We assume that there are 365 days in a year.

Open Market Rents

It is assumed that open market rent for market trading units, offices, the banks and shops increases to £10 per square foot based on current rents of comparable sites in the surrounding area. The increase will take effect from the 1st April 2010 when the majority of leases are due for renewal. (Source: Wandsworth Employment Land Study, Roger Tym & Partners and King Sturge, November 2004)

Due to the poorer condition and layout of the Railway Arches, it assumed that rents increase to £7.50 per square foot. (Source: PwC)

New lettings for the period to 31st March 2010 will be charged at £7 per square foot and at open market rates thereafter. (Source: PwC)

Open Market Rents will apply under Scenarios 2 and 4.

For Scenario 2, an additional variation will be modelled where rents from 1st April 2010 are set at £8 per square foot for core Market areas and £7 per square foot for the Railway Arches.

Target Occupancy for Scenarios 2 and 4

It is assumed that occupancy of trading units increases from 2007-08 onwards on the basis that a favourable decision by the House of Lords (following their judicial review of face-to-to face meat and fish trading) and new 10-year leases (with break clauses) attract new traders or further investment by current traders. Trading unit occupancy will increase to 95% in 2007-08 and 98% in 2008-09. New lettings for the period to 2010-11 will be charged at £7 per sq ft and at open market rents thereafter. (Discussed and agreed with the CGMA)

It is assumed that the costs associated with preparing the units for letting will equal one year's rent. Therefore, new lettings rental income has been offset by one year. (Discussed and agreed with the CGMA)

Scenario 3 - Closure Timing Assumptions

Market Closure

With the exception of four leases that run until March 2015, all market leases expire on or before the 31st March 2010. 108 leases expired on 31st March 2005. The new leases have 5-year terms or where 10-year terms were proposed, a landlord's break in 2010 was included. There are approximately 400 leases in total. It is the Authority's intention to introduce a "landlord's redevelopment" break clause at the 31st March 2010 for any new leases which extend beyond April 2010. (Source: CGMA)

It is assumed for Scenario 3 – Closure that the Market will close on 31st March 2010, recognising the potential time needed to provide for enabling legislation (it has been suggested 4- 5 years) and to coincide with the expiry of the majority of the tenants' leases. (Discussed and agreed with the CGMA)

Disposal of Site after Closure

It is assumed that following market closure the local planning authority and other relevant bodies would wish to be satisfied that no alternative operators exist before an application for redevelopment is considered. The Model adopts the conservative view that given the number of interested stakeholders and potential opposition to closure, redevelopment of the site cannot be considered until closure is beyond doubt. As a consequence, a delay of 5 years has been assumed between market closure and site disposal in order complete the redevelopment and sale programme, i.e. to conduct masterplanning and marketing, to gain planning permissions and to negotiate a sale to a third party. It has therefore been assumed that the sale of the site occurs on 31st March 2015. (Source: Drivers Jonas / PwC)

A second position has also been assumed where the Authority and Defra are able to prove quickly that no alternative market operators exist and the redevelopment and sale programme is completed shortly after closure. Under this variation, it is assumed that the sale of the site occurs in the 2010-11 financial year.

Scenario 3 - Closure Costs Assumptions

Tapering of capital expenditure prior to closure

Under Scenario 3, the Model assumes that the CGMA or King Sturge schedules are followed until the three years prior to closure. It is then assumed that annual capital expenditure falls to 75% of expected levels three years before closure (2007-08), 50% two years before closure (2008-09) and 25% one year before closure, i.e. in the year of closure (2009-10). There is no asbestos or health and safety compliance expenditure under the closure Scenario. (Discussed and agreed with the CGMA)

It is noted that the reduction of expenditure can only be justified in cases where the risks from failure of plant and systems are relatively low. Allowance would also still need to be made for mandatory / statutory elements in the work which could not be eliminated or avoided. Therefore, it is assumed that the reduced expenditure is still sufficient to cover these issues. (Discussed and agreed with the CGMA)

Level of running costs post-closure pre-sale

It is assumed that the CGMA will continue to incur certain running costs after the Markets have closed and before the site can be sold. The following percentages of current costs have been assumed (Discussed and agreed with the CGMA):

• security	75%
• water	15%
• electricity	20%
• heating	5%
• cleaning	20%
• waste	0%
• CGMA admin staff & General Admin Expenditure	15%
• Insurance	33%

Number of month's redundancy payable per year of employment

Redundancy assumes 1 month's salary is paid for every year of employment at the time of closure for current members of staff in the absence of specific conditions. (Discussed and agreed with the CGMA)

Consultancy Fees

Consultancy costs of £300k are based on the costs of privatising Horticulture Research International (HRI) in 2003-04. (Source: Defra "HRI QR Financial Expenditure")

Property Negotiation Costs

Negotiation costs of £200k have been assumed reflecting the complications of valuing and restructuring the site identified by Knight Frank (Source: Defra "HRI QR Financial Expenditure" and Knight Frank, New Covent Garden Market: Advice as to the Future Potential of the Site, June 2002)

Legal Costs associated with Lease Termination

The Model assumes legal costs of £3k per tenant. The legal costs associated with negotiation for Market closure are estimated to be £2.5-£3k per lease, with costs rising to £4k-£5k if compulsory purchase of leases is required. Where tenants hold multiple leases, it is assumed that all leases held by the tenant are negotiated at the same time and for the cost of one lease. (Source: Stephenson Harwood)

The Model assumes that there are 250 tenants. (Source: CGMA)

It is noted that where PwC has undertaken business recovery work and has acted as an Administrator / Liquidator of a business with a large portfolio of tenants, legal teams have been prepared to charge £900 per lease. An uplift to £2k - £2.5k would be expected due to the particular circumstances of the CGMA and not having all the powers of an Administrator.

Other costs associated with settlement

£100k of other costs recognising the need for advice on pensions and other areas. (Source: Defra "HRI QR Financial Expenditure")

Compensation – Lease Termination

For the purposes of calculating the compensation payable associated with terminating leases it has been assumed that all existing tenants have exceeded 14 years of occupation, therefore 2 x applicable rateable value for the s.30 notice of the Landlord and Tenant Act 1954. This represents a worse case scenario and it is assumed that an alternative site is not being offered to tenants. (Discussed and agreed with CGMA)

Compensation – Lost Income

In the PKF July 2004 report, Option 2a: Closure in 2006-07 assumed that £10 million would be payable to reimburse lease holders for lost income due to the early termination of leases in addition to the compensation above. The source was attributed to the CGMA Rent Details.

In PKF's Option 2b: Closure in 2010-11, nil compensation payable for lost income was assumed. The CGMA surmise that it was assumed that the owner would be able to exercise the "landlord's redevelopment" option under the LTA 1954 and refuse to renew the tenants' leases.

The CGMA now consider the £10 million to be modest if buying out 400 leases early.

It is not known whether the £10 million covered special compensation for business extinguishment costs for business owners aged over 60.

It is noted that additional compensation may be payable to tenants under the closure Scenario. Given that a reliable estimate of the amount cannot be made at this stage, an amount has not been included in the Model.

Service Contract Termination Compensation

It is assumed that the CGMA will manage the service contracts so that there is nil compensation payable for terminating the service contracts. (Source: CGMA)

Pension shortfall

According to the CGMA's 2004-05 audited financial statements, the net assets of the Covent Garden Market Authority Pension Plan at the 31 March 2005 amounted to £177k. Net liabilities were recognised in the previous two financial years (net liabilities of £175k in 2004 and £186k in 2003). (Source: CGMA)

However, the FRS 17 value is not representative of the cost that would arise if the pension scheme were to be wound up. A full actuarial valuation would be necessary but is not considered time or cost effective at this point in time. According to the valuation CGMA, the most recent triennial valuation was undertaken by the scheme actuary in April 2003 and the additional cost of purchasing buy-out annuities fully to cover the fund's liabilities would have been £750k. An ***informal*** rough estimate by the scheme actuary in summer 2005 would put the current cost at £1 million - £1.5 million. Therefore, the Model assumes that the cost will be £1.5 million at the time of closure. (Source: CGMA Pension Scheme Actuary)

It is noted that in the event of the scheme's closure, due consideration will have to be given to the provisions of the Pensions Act 2004.

Scenario 4 – Reform and Redevelopment Cost Assumptions

Planning Application

In order to obtain the necessary approvals in time to meet one of the conditions of the LTA 1954 break clauses, the planning applications for the construction of a new flower market on the current Pavilion site, residential land use on the old Flower Market site and affordable housing on the Entrance site will need to be submitted in 2005-06.

It is assumed that the planning process will take 3 years and cost up to £700k in 2005 prices inflated by R.P.I. The estimated planning fees comprise circa £150k for an Environmental Impact Assessment and £350k - £500k for fees relating to the three strands of the planning application. (Source: Drivers Jonas / PwC)

Legal costs associated with relocating Pavilion tenants

There are approximately 15 tenants in the Pavilion. It is assumed that the Authority is able to negotiate their relocation to other trading units in 2008-09. As for Scenario 3, it is assumed that legal costs amount to £3k per tenant. It is assumed that negotiations will take 12 months and vacant possession of the Pavilion is achieved by mid 2009-10. (Source: PwC, tenant numbers from CGMA tenancy schedule dated 29th March 2005)

Compensation payable to Pavilion Tenants

The Model assumes that the Authority negotiates the relocation of the Pavilion tenants without paying compensation. Compensation may be given in the form of rent free periods for the tenants' alternative accommodation, however, this has not been modelled. (Source: PwC)

Demolition of the Pavilion

It is assumed that the old Pavilion building will be demolished in 2009-10. The Model assumes that demolition will cost approx. £200 per square metre. Therefore, based on the Pavilion's area available for letting of 21,920 square feet / approx. 2000 m^2, demolition costs will amount to £400k in 2005 prices and inflated by R.P.I. (Source: PwC)

Construction of new flower market on former Pavilion site

It is assumed that a new flower market will be built on the site of the Pavilion and the triangular area currently used for coach parking.

Construction of the new flower market will begin from 1st April 2010. The Model assumes that construction will take 2 years and end by 31st March 2012. During the construction period, flower market tenants will be granted short-term Licenses rather than Tenancies with the same rents and service charges. (Source: PwC)

It is assumed that construction of the new flower market will cost £5.3 million based on an area of 10,250 square metres (110,330 square feet), comprising 8,750 square metres (94,184 square feet) of trading space and 1,500 square metres (16,146 square feet) of ancillary space. Total construction costs have been based on the Royal Institute of Chartered Surveyor's Building Cost Information Service average cost for steel framed new warehouses of £519 per square metre. (Source: RICS / BCIS and PwC)

The size of the new flower market has been based on the GMW report which proposed a new building of 14,580 square metres (156,938 square feet), comprising 8,750 square metres (94,184 square feet) of trading space and 5,830 square metres (62,754 square feet) of ancillary and office space. Given the current occupancy rates of the Flower Market and offices, the Model assumes a much reduced ancillary area.

Disposal of former Flower Market for residential development

It is assumed the former Flower Market site will be sold for residential development in 2012-13. (Source: PwC)

Disposal of Entrance site for affordable housing

It is assumed that the Entrance site is sold for affordable housing so that permission can be obtained for the private residential development on the site of the former Flower Market. The sale of the Entrance site will be linked to the sale of the former Flower Market and will occur in the same year in 2012-013. (Source: PwC)

Receipts from Sale of Land Assumptions

Scenario 3 – Closure

According to the Valuation Office Agency's Industrial Land Value Report, light industrial use land in nearby Merton Borough was valued at £900k per acre and land in Southwark was valued at £1.25m per acre.

The Model assumes that once the market has closed, planning restrictions will only allow business, light industrial and warehousing uses of the site. (Source: Drivers Jonas)

While premiums may be possible due to the large size of the site, the Model assumes a disposal value of £1 million per acre and a total disposal value of £56 million for the 56 acre site. (Source: Richard Haines at King Sturge)

Scenario 4 – Reform and Redevelopment

According to the Valuation Office Agency, land sold for residential use in nearby Southwark was valued at £12m per acre in 2005.

The Model assumes that the Flower Market site is sold for £10m per acre, with a total disposal value of £50m for the 5 acre site. (Source: PwC estimate based on VOA historical data)

It is assumed that potential site preparation costs have been included in the sale value.

The Model assumes that the 5-acre Entrance car park site is linked to the sale of the Flower Market site and is sold for affordable housing. It is assumed that its value has been included in the Flower Market's disposal value. (Source: PwC)

Discount Rate

The Model uses a discount rate of 3.5% in accordance with the Treasury's Green Book "A Guide to Investment Appraisal". (Discussed and agreed with the CGMA)

VARIABLE ASSUMPTIONS - MACROECONOMIC AND MICROECONOMIC ASSUMPTIONS

The following figures are time-based assumptions and can be found on the "Variable Assumptions" worksheet.

Inflation

According to HM Treasury data, the average of independent forecasts for RPI for 2005 is 2.6% and 2.5% for 2006. The Retail Price Index ("RPI") is assumed to be constant at 2.5% p.a. throughout the period. (Source: Forecasts for the UK Economy, HM Treasury, June 2005)

Rent Inflation

Rents increases at the Market have been variable. According to figures provided by the CGMA, average rents increased by 10%-26% p.a. between 1991 and 1995 inclusive. There was then a 29% reduction to the average rent for the following period to 1999 and then an increase of 39% to the average rents charged between 2000 and 2005, with another increase of 16% for current rents.

According to the November 2004 Wandsworth Employment Land Study, industrial rental values in the Wandsworth borough rose by 5.0% p.a. between December 2000 and December 2003, more than twice the average rate for London (2.3%) or the UK overall (1.9%) and over the 23 years from 1980 – 2003, industrial rental value in Wandsworth grew by 5% p.a. (Source: Investment Property Databank figures quoted in the Wandsworth Employment Land Study, Roger Tym & Partners and King Sturge, November 2004)

Current Market rents were set using the analogue formula in accordance with the lease terms and are fixed until the 31st March 2009. There is a step increase of £0.50 / sq ft for the 2009-10 financial year which is equal to a 5.4% increase in the average rent.

Therefore, the Model assumes a zero percent rent inflation until the 31st March 2009 and then a 5% increase with effect from 1st April 2009. Thereafter, it is assumed that rents increase by RPI each year although in reality rents are likely to stay flat for 3-4 years with a step increase later. (Discussed and agreed with the CGMA)

Wage Inflation

Wage inflation is assumed to be constant at 3% p.a. (i.e. 0.5% above RPI) throughout the period. (Discussed and agreed with the CGMA)

Energy Inflation

It is assumed that energy costs, i.e. electricity and heat, will increase at a constant rate of 7.5% p.a. (i.e. 5% above RPI) throughout the period. See note under Constant Assumptions above. (Discussed and agreed with the CGMA)

Water Inflation

It is assumed that water costs increase by 6.5% (i.e. 4% above RPI) for the five years to 31 March 2010 and 4% (i.e. 1.5% above RPI). See note under Constant Assumptions above. (Source: OFWAT)

Waste Disposal Inflation

It is assumed that cleaning costs increase by RPI p.a. Waste disposal costs increase at a rate of 7.5% p.a. (i.e. 5% above RPI) throughout the period. See note above under Constant Assumptions. (Source: CGMA)

Inflation of service charges as increases over RPI

The costs that are recovered via the General Service Charge and Group Service Charges inflate at different rates. Therefore, as a best estimate, it is assumed that the service charges inflate at the weighted average of these rates, i.e. 4% (or 1.5% above RPI). The relative weighting of each cost is assumed to remain broadly consistent during the period being forecast. (Discussed and agreed with the CGMA)

Direct Recoveries Inflation

It is assumed that Direct Recoveries income from tenants for metered electricity, water and Railway Arch waste increase at a constant rate of 7.5% p.a. (i.e. 5% above RPI) throughout the period. (Discussed and agreed with the CGMA)

Inflation of Car Parking Charges

It is assumed that car parking receipts increase by 5% (i.e. 2.5% above RPI) reflecting the level of increase that the CGMA would expect over a 3-year period. (Source: CGMA)

VARIABLE ASSUMPTIONS – REVENUE AND COST ASSUMPTIONS

The following figures are time-based assumptions and can be found on the "Variable Assumptions" worksheet.

GENERAL REVENUE AND COST ASSUMPTION

It is assumed that the 2005-06 CGMA budget represents the costs and revenues of a typical year in the operation of the Market. (Source: CGMA)

It is assumed that all revenue and costs assumptions are the same under each Scenario unless otherwise stated.

REVENUE ASSUMPTIONS

Rents

The 2005-06 budget for total rents amounts to £3,983k, representing a £2k / 0.05% increase on the 2004-05 outturn, and was based on the March 2005 lettings position. According to the CGMA, rental income is assumed to be static in spite of the 16% increase in rents following the 2005 rent review. This lack of growth is attributed to the £250k of 2004-05 revenue that was unique to that year, being made up of premiums paid for early lease surrenders and temporary licence fees for short lettings; the assumed net increase in lettings being offset by lower rents being charged than currently apply; and additional voids from the early lease surrenders agreed in 2004-05. (Source: CGMA Board Papers AP/05/15 and AP/05/19) (The CGMA note that evidence of the actual letting position in the 2005-06 financial year has not been encouraging, but management will endeavour to recover the position.)

Rents are expressed in 2005 prices in the Model and are escalated by rent inflation once a year on the 1st April, with the first actual increase in 2009-10 due to fixed rents until the 31st March 2009. (Source: CGMA 2005-06 budget)

Scenario 1

According to figures provided by the CGMA, Market occupancy of trading units has remained constant at just above 90% since 2001-02 (source: CGMA occupancy rate figures). Occupancy of offices has declined from 62% in 2001-02 to 46% in 2004-05. As noted above, the 2005-06 rents budget was based on March 2005 occupancy and assumed net increases in lettings although little progress has been made during the first months of the financial year. (Source: CGMA)

Scenario 1 assumes that rental income remains flat in real terms except for the increase to the petrol stations noted below. It is assumed that any further drop in office occupancy and rental income will be offset by an equal increase in income from the trading units. (Discussed and agreed with the CGMA)

Esso Petroleum ("Esso") currently leases two petrol filling stations. The two leases expire in June 2008 and July 2008 and are at a combined rent of £23.5k p.a. Under Scenario 1, it is assumed that the rent increases to £42,625 in 2005 prices from 2008-09 onwards, being 110% of its 2005 Rateable Value. As the rent increase will be effective part way through 2008-09, it is assumed that rents remain at current levels for the first 4 months and the total for the year amounts to £36.25k in 2005 prices. (Source: Valuation Office Agency 2005 Ratings List, RV for petrol filling station and premises at 54 Wandsworth Road, SW8 2 LF)

The Model does not consider the possible outcome of discussions between the CGMA and Esso regarding the construction of a Compressed Natural Gas facility on the site of the petrol filling stations.

Scenario 2

It is assumed that occupancy of trading units, including the Railway Arches, increases from 2007-08 onwards on the basis that a favourable decision by the House of Lords (following their judicial review of face-to-to face meat and fish trading) and new 10-year leases (with break clauses) attract new traders or further investment by current traders. Trading unit and Railway Arches occupancy will increase to 95% in 2007-08 and 98% in 2008-09. These new lettings for the period to 2010-11 will be charged at £7 per square foot, thereafter at open market rents. (Discussed and agreed with the CGMA)

It is assumed that the costs associated with preparing the units for letting will equal one year's rent. Therefore, new lettings rental income has been offset by one year. (Source: CGMA)

Scenario 2 assumes that from 1st April 2010, rent for market trading units, offices, the banks and shops increases to £10 per square foot based on current rents of comparable sites in the surrounding area. (Source: Wandsworth Employment Land Study, Roger Tym & Partners and King Sturge, November 2004) Due to the poorer condition and layout of the Railway Arches, it assumed that rents increase to £7.50 per square foot. (Source: PwC)

It is noted that the CGMA think that an increase of rents to £10 per square foot is optimistic.

Although office occupancy rates and rental income have declined in recent years, it is not assumed that the offices are de-rated and revenue foregone at this point. See note below for General Rates.

It is assumed that the CGMA continues to use Covent House for its office accommodation.

The increase in rents for the two Esso petrol filling stations outlined above also applies under Scenario 2.

Scenario 3

Rents are as for Scenario 1 for the period up to closure on the 31st March 2010.

It is assumed that from the 1st April 2010 to the sale of the site, the CGMA will continue to receive rental income from the non-core market areas as follows:

The Model assumes that Covent House is leased for office space at 110% of its 2005 Rateable Value, i.e. £91.52k. It is also assumed that there is an 18-month void period for marketing the office space and for a rent free period. Therefore, there are nil rental receipts in 2010-11 and 50% of expected receipts in 2011-12. (Discussed and agreed with the CGMA)

The Model assumes that income from the Railway Arches drops by 50% in the first year after closure to £218k, with a further fall to 0% in the second year as traders that were closely integrated, or highly dependent on Market activities, move away. It is assumed that occupancy recovers slightly to 25% in the third year and to 50% of current rent thereafter as new non-market users rent space. (Source: CGMA)

It is assumed that the Sunday Market continues and rental receipts continue at 2005-06 prices of £270k inflated by rent inflation. Subject to planning permission, the Sunday Market could grow larger as tenants would no longer object. (Discussed and agreed with the CGMA)

According to the CGMA management team, J Sainsbury Ltd delivery vehicles have a right of access across the site regardless of whether the market is operational (lease SGL 73044). Therefore, the Model assumes that the Main Entrance to the Market will continue to be used to gain access to the site. It is assumed that the Royal Mail and BMW continue to rent their current areas at the entrance at 2005-06 prices of £124k p.a. and £32k p.a. respectively, inflated by rent inflation which from 2010-11 onwards is equal to RPI. This inflation rate has been assumed in the absence of any formal data. (Discussed and agreed with the CGMA)

As the site remains accessible and the underground parking below the flower market is self-contained, it is also assumed that its rental income of £49k continues at 2005-06 prices, inflated by rent inflation. (Discussed and agreed with the CGMA)

The top 5 decks of the multi-storey car park, i.e. approximately one third of its area, are currently leased to BMW for £62k p.a. As the site remains accessible, it is assumed that the multi-storey car park will continue to generate income as per the 2005-06 budget, inflated by rent inflation. (Discussed and agreed with the CGMA)

It is noted that after closure, additional decks could be leased to BMW and up to £186k rent p.a. could be generated. As this increase in rental income is dependent on BMW requiring the additional space and agreeing to a 5-year Landlord and Tenant Act excluded lease, the Model does not assume this higher rent.

Rents from the flats at 33 Battersea Park Road are governed by assured short hold leases. After closure of the Market, the Model assumes that the two 1-bedroom flats currently leased to the Operations and Assistant Operations Managers will be let at open market rates of approximately £135k per week / £7k p.a. (Source: Abbey Lettings and A&M Estate Agents) Therefore, it is assumed that total rents from 33 Battersea Park Road will amount to £67.5k after closure.

The increase in rents for the two Esso petrol filling stations outlined above also applies under Scenario 3. However, after closure, it is assumed that Esso will rent only the Wandsworth Road site and therefore, rental income will fall by 50% to £21.3k from closure onwards. (Discussed and agreed with the CGMA)

As the site will remain accessible for Sainsbury's, it is assumed that Banhams will continue to rent the wayleave and parking area as per the 2005-06 budget of £26k, inflated by rent inflation which from 2010-11 onwards is equal to RPI. (Discussed and agreed with the CGMA)

Under the second variation of the closure scenario, the site is sold in the year after closure. Therefore, the above receipts will only be recognised in 2010-11.

Scenario 4

The rental income assumptions made for Scenario 2 apply under Scenario 4 with the following exceptions:

Scenario 4 assumes that occupancy rates at the Pavilion remains constant until its closure / demolition. Pavilion rents fall to 25% of current levels in 2009-10 as it is assumed that tenants agree to move to alternative units on the site before the Pavilion's demolition in mid 2009-10. It is assumed that there will be nil rents from the Pavilion thereafter. (Discussed and agreed with the CGMA)

Occupancy of the remaining fruit and vegetable trading units will increase to 95% in 2007-08 and 98% from 2008-09 as per Scenario 2 above.

During the two-year construction period of the new flower market, the flower market tenants will continue to trade from the current Flower Market and will be granted short-term licenses with the terms of their old leases, i.e. current rents and service charges. It is assumed that the occupancy rates for the old Flower Market will remain at current levels prior to its closure. (Discussed and agreed with the CGMA)

It should be noted that the Model assumes that the new cost recovery regime detailed below takes effect from the 1st April 2010 for all tenants. The continuation of the current service charges has not been modelled for the flower market traders because the difference between the current and proposed calculations is not considered material to the outcome of the financial projections.

Using the current base, an estimated £1,288k (in 2005 prices) of service charges plus an amount for direct recoveries of metered electricity etc. will be recovered from the flower market tenants in 2010-11. Under the new arrangements, it is estimated that £2,085k (in 2005 prices) of costs would fall to these tenants (approx. 20% of the recoverable costs based on the total trading area and the let office space of the current Flower Market). This represents a difference of approximately £797k of which an amount would relate to direct recoveries. Therefore, the remaining difference will not significantly affect the final projections.

It is assumed that when the new flower market opens, the tenants will be granted new leases at open market rents noted above and service charge recovery as per Scenario 2, variation c below. The Model assumes that the new flower market opens on the 1st April 2012.

Occupancy rates for the new flower market are as per the targets for Scenario 2 noted above, i.e. 95% in 2007-08 and 98% from 2008-09. As it is assumed that the new flower market opens in 2012-13, the Model uses an occupancy rate of 98%.

See note above on the size of the new flower market (under 'Constant Assumptions').

Once the former Flower Market site has been sold, there will be nil rents from the Underground Car Park. (Discussed and agreed with the CGMA)

Once the Entrance site has been sold, there will be nil rents from the Royal Mail Entrance area, the BMW Entrance area and the flats at 33 Battersea Park Road. (Discussed and agreed with the CGMA)

Total Service Charges

Total Service Charges comprise the General Service Charge ("GSC") and the Group Charges of the flower market carrying-in teams and the heating and temperature control charges. The GSC represents 91% of the total service charges income. The 2005-06 budget GSC is £10 per square foot, an increase of 6.3% on the £9.41 per square foot charge in 2004-05. The heating and temperature charges budgets increased year-on-year between 29% and 35%. Overall, the total service charges budget increased by 7.6% to £4,658k. (Source: CGMA Board Paper AP/05/15)

The current service charges calculation includes void areas, i.e. the service charge per square foot is calculated based on the total area available for letting and the CGMA then covers the amounts not recovered from vacant areas. At current occupancy rates of the fruit and vegetable units and offices, the flower market hall and offices, the amenity bridge and Link House, unrecovered GSC amounts to £1,056k (based on 105,575 vacant square feet) and unrecovered Group Charges to £127k. (Source: CGMA: occupancy rates calculated from the market areas in file Maxrent.xls dated 29 March 2005 from Colin Farey and service charge budgets)

According to the CGMA, the Service Charge formula was defined in 1978 and has remained in the lease with few amendments. According to discussions with the CGMA, the earliest opportunity for re-negotiating the service charge will be 2010 when leases are due for renewal. (Source: CGMA)

Scenario 1 and Scenario 3

Under Scenario 1 and Scenario 3, it is assumed that amounts recovered via the service charges remain at 2005-06 levels in real terms and are inflated by 4% as noted above. (Discussed and agreed with the CGMA)

After closure, it is assumed that the Railway Arches tenants pay suppliers directly for services received. (Discussed and agreed with the CGMA)

Scenario 2

The Model considers three different treatments of the service charges under Scenario 2 – Reform.

Scenario 2a

Under variation (a) of Scenario 2, amounts recovered via the service charges remain at 2005-06 levels in real terms and are inflated by 4% until 31st March 2010 and beyond because it is assumed that the service charge terms and interpretation remain unchanged. (Discussed and agreed with the CGMA)

Scenario 2b

Under Scenario 2b, it is assumed that amounts recovered via the service charges remain at 2005-06 levels in real terms and are inflated by 4% until 31st March 2010. From 1st April 2010, it is assumed that the service charge is revised and a percentage of all running costs are recovered from tenants as per current recoverability levels (see Table 1 below). From 1st April 2010, it is also assumed that the CGMA no longer covers the service charges falling to the void units and offices. It is assumed that there is a critical mass of tenants to ensure that the service charge burden does not become too onerous when dividing costs by the let area rather than the area available for letting. (Discussed and agreed with the CGMA)

It is noted that this is the CGMA considers the above to be a substantial assumption as current occupancy of the Market is approximately 81% and the CGMA believe that the critical mass of tenants needed to ensure a fair service charge burden for each tenant is 85%.

As noted above, the CGMA currently covers the service charges falling to vacant units and offices. For information, a separate calculation calculates the amounts that could fall to the CGMA if it continued to cover the service charge costs of vacant units.

For information, a separate calculation calculates the amounts that could be recovered from the tenants if a more robust approach were adopted and 98% of all expenditure, including capital expenditure, could be recovered from the tenants.

For the purpose of the Scenario 2b calculations, the Model does not make a distinction between service charges and recovery of utility costs. The specific apportionment between tenant communities has not been modelled.

Table 1: Percentage of costs recovered from tenants via the service charges and direct recoveries

The assumed recovery percentages for Scenario 2b can be found in the first column. These have been based on the current split of forecast outturn between service charge related Column A and CGMA only Column B in the June 2005 Management Accounts.

According to the CGMA, the recovery of costs incurred under the Planned Preventative Maintenance Programme depends on the split between revenue and capital expenditure. As a general rule, major refurbishment or replacement works are capitalised with recovery of plant–related expenditure via depreciation. (Depreciation of buildings is not included in the GSC calculation.) Maintenance work is classified as revenue expenditure and may be recovered from the tenants. (Source: CGMA)

43% of the CGMA's 3-year capital expenditure programme will be recoverable from tenants. (Source: CGMA)

Based on CGMA analysis of the King Sturge programme, it is assumed that 23% of the total programme will be recoverable from the tenants. The model makes no distinction between the different types of costs or fluctuations in recoverable costs year-on-year. CGMA analysis of the Emergency Repairs proposed by King Sturge concluded that £589k / 89% of the net cost would be recoverable. (Source: CGMA)

These percentages do not take into account ongoing discussions between Defra and the CGMA on the recoverability of maintenance and repair expenditure from the tenants.

Scenario 2c assumes a high recovery rate but the CGMA will cover the void trading units. See note below.

	SCENARIO 2b ("2b – Recoverable Costs WP")	SCENARIO 2c ("2c – Recoverable Costs WP")
STAFF COSTS		
CGMA Members Emoluments	0%	0%
Salaries and Pension Contributions – Admin	0%	0%
Salaries and Pension Contributions – Commercial	0%	100%
Salaries and Pension Contributions – Operations	100%	100%
Salaries and Pension Contributions - Carrying in gang & Dock Controller	100%	100%
SERVICE CONTRACTS		
Contract Security	99%	100%
Cleaning and Waste Disposal	99%	100%
GENERAL RATES		
General Rates Covent House	0%	0%
General Rates - Vacant Units, Advertising, Residual Areas	99%	100%
UTILITIES		
Water Rates	97.5%	100%
Electricity: Supplier: British Energy 4.044 pence / kwh + 0.43 pence / kwh climate change levy = 4.474 pence / kwh	99.5%	100%
Heating: Gas and Oil, Gas supplier: E.On 1.9716 pence / kwh	98.5%	100%
GENERAL ADMIN EXPENDITURE		
Insurance	99%	100%
GENERAL EXPENSES		
Post, Telephone, Printing	41%	41%
Marketing and Publicity	38%	38%
General Expenses	46%	46%
Reletting Costs	0%	0%
Health & Safety Compliance	0%	0%

Professional Fees	29%	29%
Audit Fee	19%	19%
Professional Advice & special study in 2006	0%	0%
Bad Debt Provision	0%	0%
Deferred Income Adjustment	100%	100%
DEPRECIATION		
Depreciation – Plant	82%	0%
Depreciation – Buildings	0%	0%
ONGOING MAINTENANCE, REPAIRS, RENEWALS & MAJOR REPAIRS		
Maintenance	91%	100%
Major Repairs	100%	100%
CGMA 3-YEAR CAPEX SCHEDULE	43%	100%
EMERGENCY REPAIRS AND WIND AND WATERTIGHT REPAIRS	89%	100%
PLANNED PREVENTATIVE MAINTENANCE PROGRAMME - SCENARIO 2 - RECOVERABLE FROM TENANTS		
Link House – Fabric	23%	100%
Link House - M & E	23%	100%
Link House – Lifts	23%	100%
Multi-storey car park – fabric	23%	100%
Multi-storey car park - M & E	23%	100%
Covent House – fabric	23%	0%
Covent House - M & E	23%	0%
Fruit & Vegetable Market – fabric	23%	100%
Fruit & Vegetable Market - M & E	23%	100%
Fruit & Vegetable Market – Lifts	23%	100%
Flower Market – fabric	23%	100%
Flower Market - M & E	23%	100%
Flower Market – Lifts	23%	100%

Pavilion – fabric	23%	100%
Pavilion - M & E	23%	100%
Railway Arches – fabric	23%	100%
Railway Arches - M & E	23%	100%
Boiler House – fabric	23%	100%
Boiler House - M & E	23%	100%
Externals – fabric	23%	100%
Externals - M & E	23%	100%
CGMA ASBESTOS & H&S WORKS (As for 3-year schedule above)	43%	100%

Scenario 2c

Scenario 2c assumes that amounts recovered via the service charges remain at 2005-06 levels in real terms and are inflated by 4% until 31st March 2010. From the 1st April 2010, it is assumed that the service charge terms and formula are renegotiated and 100% of all relevant costs, including capital expenditure, are recovered from the tenants. The percentage of costs recovered is detailed in the above table. As it is assumed that all maintenance and capital costs are recovered from the tenants, nil depreciation is recovered to avoid recharging the costs twice.

From the 1st April 2010, it is also assumed that the CGMA covers the service charges falling to the void trading units only. It is assumed that the vacant offices are no longer part of the service charge calculation. (Discussed and agreed with the CGMA)

For the purpose of the Scenario 2c calculations, the Model does not make a distinction between service charges and recovery of utility costs. The specific apportionment between tenant communities has not been modelled.

Scenario 4

Scenario 4 assumes that the recovery of Market running and capital costs is as per Scenario 2c above.

Direct Recoveries

The CGMA buys electricity in bulk at 33,000 kV from suppliers and transforms it down to 415v and 240v for use on the site. Most tenants have electricity meters and costs are re-charged to tenants based on actual consumption at the standard business rate charged by London Electricity for an equivalent supply. The difference between this rate and the discounted buying-in rate secured by the CGMA represents a "profit" which is credited to the GSC calculation, thereby reducing amounts recoverable from tenants for services. (Source: CGMA)

Tenants using large quantities of water, such as catering processors, have water meters and are charged for water consumed at £0.6548 per cubic metre. The water charges for low-usage non-metered tenants are recovered via the General Service Charge (approximately £78k per the CGMA 2005-06 budget).

Waste disposal costs for the Railway Arches (£140k per the CGMA 2005-06 budget) are recovered directly from the tenants as the majority are catering processors and produce more waste. Costs are allocated according to the weight of waste produced. Almost all of the remaining £1.9 million cleaning and waste costs are recovered via the General Service Charge (99%).

Scenario 1

Under Scenario 1, the Model assumes that Direct Recoveries continue at 2005-06 levels of £1,235k and are inflated by the Direct Recoveries inflation rate of 7.5%. (Discussed and agreed with the CGMA)

Scenario 2

Under Scenario 2, it is assumed that Direct Recoveries will continue at 2005-06 levels inflated by the Direct Recoveries inflation rate of 7.5% until 31st March 2010. Thereafter, the Model considers three different assumptions.

Scenario 2a

Scenario 2a assumed that Direct Recoveries continue at 2005-06 levels inflated by the appropriate inflation rate until the project end.

Scenario 2b

For Scenario 2b, it is assumed that from the 1st April 2010 a percentage of all Market running costs are recovered from tenants as per the current General Service Charge / Authority split. For the purpose of the Model calculations, a distinction has not been made between service charges and direct recoveries. (Discussed and agreed with the CGMA)

Scenario 2c

As noted above for service charges under Scenario 2c, it is assumed that from the 1st April 2010, 100% of all relevant costs are recovered from the tenants. No distinction has been made between service charges and direct recoveries. (Discussed and agreed with the CGMA)

Scenario 3

For the period to the closure of the Market, Scenario 3 assumes that Direct Recoveries continue at 2005-06 levels of £1,235k and are inflated by the Direct Recoveries inflation rate of 7.5%. (Discussed and agreed with the CGMA)

After closure, it is assumed that the Railway Arches tenants pay suppliers directly for services received.

Scenario 4

Recovery of Market expenses is as per Scenario 2c above.

Commercial Vehicle Charges

Commercial Vehicle charges relate to season permits and casual entry charges. It is assumed that revenues continue at 2005-06 levels of £1,163k, inflated by RPI each year. (Discussed and agreed with the CGMA)

Nil receipts are assumed after closure. (Discussed and agreed with the CGMA)

Car Parking Charges

Car Parking Charges relate to coach parking and comprises casual receipts as well as known receipts from National Express, Chalkwell and Eurolines. It is assumed that revenues continue at 2005-06 levels of £273k, inflated by 5% each year in line with the CGMA's expectations. (Source: CGMA)

Under Scenario 3 – Closure, it is assumed that £25k for Market-related parking would not continue. Therefore, it is assumed that the site generate £248k from car parking charges after closure, of which

£208k relates to coach parking. (Source: CGMA)

It is noted that £40k of budgeted car parking charges relates to a contract with Lambeth Borough Council for parking which has not yet been signed. The CGMA assume that it will be signed in the near future.

Scenario 4 assumes that a new flower market is constructed on the site of the Pavilion and the triangular area currently used for coach parking. Therefore, nil car parking charges once construction begins. (Discussed and agreed with the CGMA)

Miscellaneous Income & Interest from Market Activities

Miscellaneous income is received from a range of sources, e.g. filming receipts, a Mercedes Benz lorry demonstration. It is assumed that miscellaneous income receipts continue at 2005-06 levels of £26k inflated by RPI each year. (Discussed and agreed with the CGMA)

Nil receipts are assumed after closure. (Discussed and agreed with the CGMA)

Interest from Market Activities

The Authority earns interest on balances held in the CGMA's clearing bank and funds invested.

At the 30th April 2005, £6.435m attributable to the market was invested in a range of interest-bearing funds. In accordance with instructions from the Board, funds are invested only in the top 10 building societies and banks that were formally building societies. The CGMA uses the placement services of Preborn Marshall Yamani. (Source: CGMA Board Paper AP/05/21)

According to the CGMA, the investments held are made up of a combination of cash sources, not all of which would be automatically claimable by Defra. Defra's agreement to using the CGMA's funds for capital investment relates primarily to the retained annual surpluses, but the Authority would be able to use more of its funds for this purpose if it was considered necessary and prudent to do so. The CGMA noted that the funds held at the end of April 2005 were high because certain large payments were due shortly afterwards, e.g. the insurance premium. The CGMA projects funds to fall to £4.5 million by March 2006. (Source: CGMA)

The Model assumes that interest earned continues at 2005-06 levels of £188k. Interest has not been inflated because it is assumed that inflation is taken into account in the interest already. (Discussed and agreed with the CGMA)

If the CGMA remained in existence after closure of the Market, it would need to retain a certain amount of working capital but not the same level of funds held currently. It is therefore assumed that the majority of funds have been used for capital expenditure prior to closure or have been surrendered to Defra. It is assumed that any interest earned on the working capital held is not material and has not been included in the model. (Discussed and agreed with the CGMA).

The tenants' deposits are held in an Escrow account in the joint CGMA / tenants names. All interest earned is paid over to the tenants or rolled up in the deposit. This interest has not been included in the model. If tenants default on their obligations to the CGMA, the monies held go to the CGMA. These receipts have been taken into account by the CGMA when calculating the bad debt provision. (Source: CGMA)

Interest earned on funds invested following the sale of Market Towers

According to the 2004-05 financial statements, the CGMA has a responsibility to pay a special dividend to Defra after the year ended 31 March 2011. This relates to the Market Towers Contingent Liability Fund established in 1989 on the sale of the Market Towers office block.

The Fund currently amounts to £3,258k, with the expected dividend payable to Defra amounting to £2,558k. The CGMA expects to retain the difference of £700k, being equal to the Corporation Tax paid by the CGMA on interest earned on the Fund, and interest. (Source: CGMA)

The Fund is currently loaned to Bolton Borough Council on a 3-month fixed rate of 4.76%. (Source: CGMA)

The cash flow relating to the Fund has not been included in the model.

COST ASSUMPTIONS

Staff Costs

Staff Costs comprise salaries and pension contributions for Administration, Commercial and Operations staff as well as the team of porters at the Flower Market and the Dock Controller. CGMA Board Members emoluments have also been included.

The 2005-06 budget of £1,740k represents a 5.7% increase on the 2004-05 outturn. The annual pay increase accounts for 3.6% and the CGMA attributes the further rise to the full complement of Board Members, increased pensions contributions, the return of a member of staff from maternity leave and the overlap of the new and former Commercial Manager. (Source: CGMA)

Under Scenario 1 – Status Quo and Scenario 3 – Closure, it is assumed that staff costs continue at 2005-06 levels of £1,740k, inflated by wage inflation of 3% each year. (Discussed and agreed with the CGMA)

Under Scenario 2 – Reform and Scenario 4 – Reform and Redevelopment, it is also assumed that the staffing levels will continue at 2005-06 levels as, according to the CGMA, staffing levels are already at the minimum required to maintain Market activities at current levels. (Source: CGMA)

Service Contracts

We have been informed that the CGMA has entered into contracts with two contractors to provide security services and cleaning and waste disposal services. The security contract was renewed in 2004 with CIS Security Ltd for 2 years and is due to expire in August 2006. The 2005-06 budget of £853k is £48k / 6% higher than in 2004-05. The higher budget reflects a full financial year at the new price and some additional manpower resources for increased enforcement duties. (Source: CGMA Board Paper AP/05/15)

The cleaning and waste disposal contract is a 5-year contract with MacLellan and the waste contract has been sub-let to Sita. The contract commenced in August 2003 and will expire in August 2008. The 2005-06 budget of £2,036k was set £55k / 2.8% above the 2004-05 outturn, thereby allowing for inflation. The CGMA consider that this is a challenging target to meet. (Source: CGMA Board Paper AP/05/15)

It is assumed that security and cleaning costs increase by RPI p.a. and waste disposal costs increase at a rate of 7.5% p.a. (i.e.5% above RPI) throughout the period. See note above under Constant Assumptions. (Source: CGMA)

Under Scenario 3 – Closure, it is assumed that the amount of security required during the period between closure of the markets and the sale of the site will equal 75% of current levels. It is assumed that the site will remain open to allow access to the Sainsbury's delivery vehicles and other ongoing users of the site as outlined above. It is assumed that cleaning costs will continue to be incurred at 20% of current levels in order to maintain a tidy site. No waste disposal costs will be incurred by the Authority. It is assumed that the tenants of the Railway Arches will pay directly for these services after closure. (Discussed and agreed with the CGMA)

General Rates

The tenants pay general rates directly to the relevant local authority, in this case the London Borough of Wandsworth. The CGMA is required to pay 50% of the rates of empty non-trading premises with a Rateable Value greater than £2.2k, with 100% relief on the rates of empty trading premises. (Source: Valuations Office Agency)

According to the CGMA, the empty rates are partially recovered via the GSC. (Source: CGMA)

The rates for Covent House amount to £35k. (Source: CGMA)

The rates payable by the CGMA are as per the 2005-06 CGMA budget. (Discussed and agreed with the CGMA)

It is noted that the 2005-06 budget is based on the 2000 Rateable Values. At the time of producing the Model, the CGMA had not updated their records with the new values. As the budget for General Rates amounts to only £135k, any difference between the budget and the actual rates payable is unlikely to be material to the financial projections.

The Rateable Values are revised every five years. Instead of a step increase to the rates payable every five years, the Model assumes that general rates increase annually by RPI. (Source: Gerald Eve)

According to the CGMA, the offices are leased by a core group of tenants that are expected to stay at the Market. Although the CGMA is obliged to pay the unrelieved rates of the vacant offices, the Model assumes that these offices will not be de-rated at this point and therefore general rates will be payable in the future.

It is noted that Gerald Eve has lodged an appeal with the Valuations Office Agency seeking to make the vacant offices non-rateable. A decision is expected by the end of 2005. If the appeal is not successful, Gerald Eve may look into other ways to de-rate the offices, e.g. by removing the office façade and removing services so that beneficial occupation is no longer possible. (Gerald Eve)

After closure of the Market but before the disposal of the site under Scenario 3, it is assumed that the CGMA would continue to pay rates for all the vacant offices with Rateable Values above £2.2k and to receive relief of 50%. There would be 100% in the first three months of the office space becoming vacant. There is 100% relief on rates payable on the vacant trading units. (Source: Valuations Office Agency)

As the total number of offices with Rateable Values above £2.2k is not readily available, it is assumed that the CGMA continues to pay rates in line with the 2005-06 budget as any difference will not be material.

Utilities

Water

In 2004-05, actual water charges of £133k were incurred. The 2005-06 budget forecasts water charges of £123k based on the CGMA's estimate of tenants' water usage. The fall in usage is attributed to a burst pipe in 2004-05. (Source: CGMA)

It is assumed that water consumptions remains at 2005-06 levels and costs are inflated by 6.5% up to 31st March 2010 and 4% thereafter as outlined above. (Source: OFWAT & discussed and agreed with the CGMA)

Under Scenario 3 – Closure, it is assumed that between closure of the markets and the sale of the site water consumption will fall to 15% of its current levels, i.e. approximately £18k in 2005 prices inflated by the inflation rates above. (Source: CGMA)

Electricity

We have been informed that the 36% increase on the 2004-05 outturn for the 2005-06 budgeted electricity costs was due to a 28% increase to contract base price as well as the imposition of a new levy, similar to the climate change levy, by the government and an increase in metered consumption by tenants in line with trends. (Source: CGMA Board Paper AP/05/15)

As noted above, while energy prices have risen significantly in the past few years, it is assumed that over the long-term price increases will represent a steady increase. The Model assumes that electricity prices continue at 2005-06 prices at £1,036k, inflated annually by 7.5%, i.e. a rate of inflation 5% above RPI based on historical data from the DTI. (Discussed and agreed with the CGMA)

Under Scenario 3 – Closure, it is assumed that between closure of the markets and the sale of the site electricity consumption will fall to 20% of its current levels, i.e. approximately £207k in 2005 prices inflated by 7.5% as noted above. (Discussed and agreed with the CGMA)

Heating

The 2005-06 heating budget of £272k is £109k / 67% higher than the 2004-05 outturn. The increase is attributed to higher oil and gas charges as well as allowing for a 'cold' winter contingency. (Source: CGMA Board Paper AP/05/15) It is noted that the contingency element has already been used as actual costs to-date have been higher than expected. (Source: CGMA)

It is noted that there have been substantial increases to oil and gas prices recently. It is assumed that over the medium- to long-term, prices will increase at a steady rate just above inflation. Therefore, the Model assumes that heating costs continue at 2005-06 forecast prices of £272k, inflated annually by 7.5%, i.e. a rate of inflation 5% above RPI. (Discussed and agreed with the CGMA)

Under Scenario 3 – Closure, it is assumed that between closure of the markets and the sale of the site heating consumption will fall to 5% of its current levels, i.e. approximately £14k in 2005 prices inflated by 7.5% as noted above. (Discussed and agreed with the CGMA)

Insurance

We have been informed that the CGMA secured a reduction in the annual insurance premium payable during 2005-06 due to previous health and safety work and the upgrade of the sprinkler system. For Scenarios 1 and 2, it is assumed that the 2005-06 risk profile of the Market remains the same and that maintenance and capital expenditure is sufficient to cover additional health and safety requirements. Therefore, the Model assumes that insurance premiums of £775k p.a. continue at 2005-06 prices, inflated annually by RPI. (Discussed and agreed with the CGMA)

Under Scenario 3 – Closure, it is assumed that insurance costs before closure are as above and between closure of the markets and the sale of the site, the annual insurance premium will fall to 33% of its current level, i.e. approximately £258k in 2005 prices inflated by RPI. This is based on continued public liability cover, some cover of the Market fabric and structures and clean-up cover. Interruption of business would no longer be required. (Discussed and agreed with the CGMA)

General Admin Expenditure

General Expenses comprise the following costs:

- Post, Telephone, Printing
- Marketing and Publicity
- General Expenses
- Reletting Costs
- Health & Safety Compliance
- Professional Fees & Advice
- Audit Fee

The 2005-06 budget forecast total general expenses of £930k, some £81k above the 2004-05 outturn. A £80k budget for the judicial review and the Market disposal project accounts for most of this increase. According to the CGMA, both will recur in 2006-07 at an estimated combined cost of £100k. (Source: CGMA)

The Model assumes that General Admin Expenditure ("GAE") continues in the future at 2005-06 prices, inflated by RPI. It is assumed that the special study occurs in 2005-06 and 2006-07 only. (Discussed and agreed with the CGMA)

Under Scenario 3 – Closure, it is assumed that between closure of the markets and the sale of the site the CGMA will continue to incur up to 15% of its current GAE and Admin staff costs, i.e. approximately £250k in 2005 prices inflated by RPI and wage inflation respectively. (Discussed and agreed with the CGMA)

Additional one-off costs not included within General Expenses

It is noted that the Authority may have to meet legal costs if the CGMA and Defra lose their appeal to the House of Lords regarding face-to-face sales of meat and fish at the Nine Elms site.

The CGMA estimates costs of £250k may be payable to cover the cost of the petition and the Corporation of London's costs – representing 50% of total estimated costs with Defra meeting the other 50%. (Source: Mike Liggins estimate 29 June 2005) However, this cost has not been included in the model.

Bad Debt Provision

The 2005-06 budget forecasts a bad debt provision of £70k compared to the actual provision of £31k in 2004-05. The provision was increased to reflect the greater potential for rental bad debts following the 2005 rent review. (Source: CGMA Board Paper AP/05/15)

The Model assumes that the annual provision for bad debts continues at 2005-06 levels, inflated by RPI. (Discussed and agreed with the CGMA)

Deferred income Adjustment

We have been informed that previous surpluses generated from general service charge receipts were credited to a deferred income account rather than being reimbursed to the tenants. When the costs included in the service charge calculation exceeded receipts, a deferred income adjustment would cover the shortfall. As a result, the tenants would not face significant changes to the annual service charge.

We have been informed that the Authority is currently running down the Deferred Income Account with the intention of reducing its balance to a nil balance. According to the Authority, the current balance is £255k. (Source: CGMA)

The Model assumes that there are two deferred income adjustments to reduce the balance to zero – one in 2005-06 of £100k as per the 2005-06 budget and another of £155k in 2006-07. (Source: CGMA)

Depreciation

A total annual depreciation charge of £611k is expected in 2005-06. It is assumed to continue at this level in the future and has been included in the model to calculate net surplus / (deficit) before tax. It is noted that a proportion of the expenditure under the Planned Preventative Maintenance Programme may be capitalised and therefore the annual depreciation charge may increase.

Total depreciation is then added back and depreciation on the roof only is deducted as it is assumed that this is equal to the Capital Allowances for tax purposes and therefore tax is calculated on the net surplus after depreciation of the roof. The depreciation charge for the roof amounts to £295k per annum. (Source: CGMA)

Depreciation has been included in the Model as an approximation of Capital Allowances for tax purposes only. The depreciation charge is then added back to the net surplus / (deficit) so that the free cash flow can be calculated. Given the amounts involved, it is assumed that the increase in depreciation / Capital Allowances due to the Planned Preventative Maintenance Programme and the impact on the tax payable is not significant.

Ongoing Maintenance Repairs and Renewals

It is assumed that the 2005-06 maintenance, repairs and renewals budget of £1,325k continues, inflated annually by RPI to reflect expected increases in the cost of materials. (Source: CGMA Board Paper AP/05/15)

According to an email [redacted] dated 27 June 2005, dilapidation costs for the financial years ending 31 March were as follows:

2002-03	£20,459
2003-04	£32,469
2004-05	£ 7,960
2005-06	£12,000 (budget)

It is assumed that £12k dilapidation costs will continue in the future, inflated by RPI. (Discussed and agreed CGMA)

The 2005-06 budget includes £605k for Major Repairs. According to the CGMA, the split between Major Repairs and Maintenance and Repairs is for management accounts purposes with the intention of demonstrating to the tenants that significant works are being undertaken on the Market. (Source: CGMA)

Under Scenario 1a, it is assumed that the King Sturge programme will not be followed and ongoing maintenance costs remain at 2005-06 levels, i.e. £1,942k. (Discussed and agreed with the CGMA)

When the King Sturge Planned Preventative Maintenance Programme is adopted, the Model assumes that the need for a Major Repairs budget is reduced and only £150k p.a. will be required. (Source: CGMA)

Under all Scenarios excl. 1a, the King Sturge maintenance programme is adopted after the CGMA's 3-year capital expenditure plan (see note below). Therefore, total ongoing maintenance costs for all Scenarios amount to £1,942k inflated annually by RPI until 2009-10 and £1,487k (i.e. maintenance, dilapidations and reduced Major repairs) in 2005-06 prices, inflated annually by RPI thereafter. (Discussed and agreed with the CGMA)

Emergency Repairs and Wind and Watertight Repairs

As part of their "Planned Preventative Maintenance Programme of New Covent Garden Market" report, King Sturge undertook an assessment of repair and refurbishment required to the site to maintain the premises in wind and watertight condition for the three years from 2005-06 to 2008-09.

The Model assumes that the Authority completes this programme under each Scenario, with work commencing in 2006-07. Therefore the King Sturge figures have been offset by one year. (Source: King Sturge)

Professional fees of 12% are added to the net costs. As the costs are quoted in 2005 terms, the costs are inflated annually by RPI. (Source: King Sturge)

VAT has not been added to the net cost as the CGMA is able to reclaim all VAT. (Source: CGMA)

Ongoing Capital Expenditure and Backlog Capital Expenditure

The Model assumes a capital budget of £1,570k in 2005-06. This represents the total capital expenditure funding available for 2005-06 as per the CGMA Board Paper AP/05/16. (Source: CGMA Board Paper AP/05/16)

According to the CGMA Board Paper AP/05/16, the £1,570k comprises routine ongoing capital expenditure of £296k. Therefore, backlog maintenance of £1,274k is assumed. The £575k Defra funding for capital expenditure has been included in the model. (Source: CGMA Board Paper AP/05/16)

From 2006-07, it is assumed that the Authority will follow the 3 year capital expenditure programme prepared in July 2005 (source: CGMA) and inflated by RPI (discussed and agreed with the CGMA). The 3-year programme comprises:

Year	CGMA Capital Expenditure Plan
2006-07	£1,597k
2007-08	£2,147k
2008-09	£2,122k

From 2009-10, the King Sturge Planned Preventative Maintenance Programme will be followed. (Source: King Sturge)

It is assumed that there will be sufficient funds to finance the capital expenditure. It may be necessary for the CGMA to use some, or all of its funds held to meet the cash outflow in the short-term.

Planned Preventative Maintenance Programme

King Sturge's March 2005 report "Planned Preventative Maintenance Programme of New Covent Garden Market" estimates the level of expenditure on fabric and services repair and maintenance work required each year over the 15-year period from 2005-06 to 2019-20.

The report does not include an assessment of the below ground surface and foul drainage systems and the estimated costs do not include those relating to the normal routine preventative maintenance of the building services installations.

It is noted that the CGMA estimate additional costs of £3 million relating to asbestos removal and £250k for compliance with health and safety regulations that were not included in the King Sturge report. According to the CGMA, the costs associated with repairing / maintaining the drainage systems would be substantial although no estimate has been made of the costs. (Source: CGMA)

Moreover, it is noted that the CGMA considers that major investment would be needed in the following areas if market activities continue in the longer-term:

- Waste disposal
- Roads
- Site security
- New warehousing
- New chilling facilities
- Office refurbishment
- General "face-lift"

The Model assumes that the Authority undertakes the works proposed in the King Sturge Planned Preventative Maintenance Programme. It is assumed that work commences in 2009-10 after the period covered by the CGMA's own budget estimates and therefore the King Sturge figures have been offset by 4 years. (Source: King Sturge)

Professional fees of 12% are added to the net costs. As the King Sturge planned costs are quoted in 2005 terms, the costs are inflated annually by RPI. (Source: King Sturge)

VAT has not been added to the net cost as the CGMA is able to reclaim all VAT. (Source: CGMA)

It is assumed that the CGMA follow a 10-year £3 million asbestos removal programme starting after the period covered by the CGMA 3 year capital expenditure programme prepared in July 2005. It is assumed that the CGMA incurs annual asbestos removal expenditure of £300k p.a. in 2005 prices, inflated by RPI for 10 years. (Discussed and agreed with the CGMA)

It is assumed that the £250k for health and safety compliance is needed in 2006-07 and £50k thereafter. It is assumed that these amounts have been included in the 3 year capital expenditure programme prepared in July 2005. From 2009-10, it is assumed that the CGMA incurs health and safety expenditure of £50k p.a. in 2005 prices, inflated by RPI. (Discussed and agreed with the CGMA)

There are two exceptions to these assumptions:

It is assumed that no work from the Programme is undertaken for Scenario 1a as it is assumed that there is insufficient funding for this expenditure. Scenario 1b assumes that the Programme is followed in full. (Discussed and agreed with the CGMA)

As noted above under Constant Assumptions, Scenario 3 assumes that the CGMA or King Surge schedules are followed until the three years prior to closure. It is then assumed that annual capital expenditure falls as per table below. There is no asbestos or health and safety compliance expenditure. (Discussed and agreed with the CGMA)

Revised CGMA / Planned Preventative Maintenance Programme Prior to Market Closure in 2010

Percentage of Programme	CGMA: 3 –year schedule of work	King Sturge – PPMP & CGMA Asbestos / H&S
4 – years prior to closure 100%	£1,597k*RPI	CGMA
3 – years prior to closure 75%	75%*£2,147 = £1,610*RPI	CGMA
2 – years prior to closure 50%	50%*£2,122k = £1,061*RPI	CGMA
1 – year prior to closure 25%	KS	25%*£1,902.49+£350k = £563k*RPI

MARKET AREA ASSUMPTIONS

It is assumed that the area available to let and the let areas remain as per the rental income spreadsheet dated 29th March 2005 (Maxrent.xls) supplied by Colin Farey of the CGMA to PwC on the 23 June 2005. (Source: CGMA)

REDUNDANCY COSTS

The CGMA provided a list of staff names, dates of birth, CGMA start dates and current salaries as at 12 July 2006. (Source: CGMA)

CGMA employees may chose to retire at 60 years old but they are entitled to work until 65. For the purposes of calculating the estimated redundancy payments for Scenario 3 – Closure, it is assumed that women and men chose to retire at 65. It is assumed that employees reaching 65 before closure of the Market have retired. (Discussed and agreed with the CGMA)

It is also assumed that staff salaries increase by wage inflation of 3% each year. (Discussed and agreed with the CGMA)

Appendix B: Financial model Output Sheet

NEW COVENT GARDEN MARKET

FORECAST NET PRESENT VALUES AT 31 MARCH 2005

Scenario	Description	£'000
Scenario 1a	Status Quo without King Sturge Planned Preventative Maintenance Programme	7,345
Scenario 1b	Status Quo with King Sturge Planned Preventative Maintenance Programme	(271)
Scenario 2a	Reform (Rents Only)	8,496
Scenario 2b	Reform (Rents + GSC)	17,848
Scenario 2c	Reform (Rents + 100% GSC)	26,236
Scenario 3	Closure	22,390
Scenario 4	Reform and Redevelopment	49,934

Report and Accounts	(2001-02 – 2004-05)
UK Wholesaling and Cash and Carry	Mintel (2005)
Houseplants and Cut Flowers Market Research	Mintel (2004)
Hotels in the UK	Euromonitor (2004)
Restaurants and Cafés in the UK	Euromonitor (2004)
The Future of Employment Land and Premises in Wandsworth	Roger Tym & Partners (2004)
Report of the Borough Planner on a report prepared by consultants Roger Tym & Partners on the future of employment land and premises in Wandsworth (Paper no. 05-268)	Wandsworth Borough Council (2005)
Report of the Borough Planner on the Local Development Framework for the Borough	Wandsworth Borough Council (2005)
Wandsworth Unitary Development Plan	Wandsworth Borough Council (2003)
The London Plan	Greater London Authority (2004)
Forecasts for the UK Economy	HM Treasury (2005)

Appendix E: Expressions of Interest.

The Authority and Defra have received a number unsolicited Expressions of Interest although no formal marketing of the site was undertaken. The fact that 15 Expressions were received indicates that a well planned disposal with an appropriate marketing campaign would generate strong interest.

The Expressions of Interest are listed in alphabetical order of the interested party.

[redacted] [redacted]

On behalf of... Arlington Securities Ltd

Summary of Business

- Privately owned UK registered company.
- Principal shareholders = Prudential Insurance Company of America, Legal & General, Abu Dhabi Investment Authority.
- Prior to 1998 was wholly owned subsidiary of British Aerospace PLC.
- Business = Development and post-occupancy management.
- Experience of integrated mixed use and sustainable developments
- Currently holds investment portfolio valued at £650m.
- Financials for y/e Dec 2003:
  - Turnover = £52.5m (£96m, 2002)
  - Pre-tax profit = £71m (£5.4m, 2004)
  - Tangible Fixed Assets = £25m (£686m, 2002)

Date of Interest June 2003

Summary of Proposal Partner/purchaser of site, maximising on going potential as market based operation, and providing redevelopment opportunities over time.

Other Information Auditors = PwC

[redacted] [redacted]

On behalf of... Comer Group (Brookstream Properties)

Summary of Business **Brookstream Properties**

- Medium size unquoted company
- Development and selling of real estate.
- Directors = Luke and Brian Comer
- Financials for y/e 30th June 2004

- Gross profit = £7m (£6.5m, 2003)
- Pre tax profit = £2m (£3.7m, 2003)
- Net assets = £10.8m (£9.4m, 2003)

Date of Interest May 2003

Summary of Proposal

- Purchase of market freehold, with market as a going concern.
- Offer of £40m (2003), to be allocated firstly against liabilities in relation to the repair and capex require, and secondly to the requirements of the sponsoring department, Defra.
- Would be prepared to create a composite market.
- Accepts principle of sharing the site with Smithfield Meat Market and Billingsgate Fish Market.
- Offer is unconditional and not dependent on any form of planning application.

Other

- Specialist Retail Operations team, who would form a Tenants Partnership.
- Initial offer made 2003. Interest and proposal confirmed in 2005.

[redacted] [redacted]

On behalf of... English Partnerships

Summary of Business

- Advisor on brownfield land, creating communities, supporting urban renaissance.
- Projects include Market Renewal Pathfinders, Millennium Communities and Urban Regeneration Companies.
- Financials for y/e 31st March 2005:
    - Income = £175m (£128m, 2004)
    - Surplus = £65m (£75m, 2004)
    - Net assets = £580m (£514m, 2004)

Date of Interest July 2003

Summary of Proposal

- Role would be strategic development partner to the Authority.
- Provision of funding for site preparation and infrastructure works.
- Provision of funding for affordable housing.
- Proceeds would be shared dependent on investment (Authoritys investment being pre development land and buildings, EPs investment being cost of items above).

  Or
- Outright acquisition of land at current market value with overage payment when developed if Authority's preference is for an early exit strategy.

Other

- Able to invest in infrastructure at an early stage, generating better financial return in the long run.
- Able to deliver policy driven regeneration objectives due to public sector credibility.

Interest expressed by... **Geraud (UK) Ltd** [redacted]

On behalf of... Geraud (UK) Ltd

Summary of Business

- Small unquoted company filing modified balance sheet only.
- Parent company = Groupe Geraud, largest operator of local authority markets in Europe.
- Current UK markets situated in Liverpool, Cheltenham, Clevedon.
- Net assets = £(1.2m) for y/e 31st March 04 (Geraud UK)

Date of Interest July 2003

Summary of Proposal Expression of interest only.

Interest expressed by... **Glenmorison Group** [redacted]

On behalf of... Glenmorison Group

Summary of Business

- Property Development
- Current projects include redevelopment of New Smithfield Market in Manchester – identifying compatible development solutions that realise the commercial value of the site to allow redevelopment of the market operation.
- Private limited with share capital
- No financial information available.

Date of Interest July 2003

Summary of Proposal Expression of interest given only

Interest expressed by... **Hines UK** [redacted]

On behalf of... Hines UK

Summary of Business

- Development and selling of real estate.
- Small unquoted company.
- Private limited with share capital.
- Modified balance sheet filed only.
- Ultimate holding company = Hines International Real Estate Holdings Ltd Partnership.
- Financials at 31st December 2003:
    - Long term liabilities = £5.8m (£4.6m, 2002)
    - Net assets = £(5.5)m (£(4.3)m, 2003)
    - Long term finance obtained from Parent Company

Date of Interest July 2003

Summary of Proposal Expression of interest in relation to market site.

Interest expressed by... **Land Securities Group**

On behalf of... Land Securities Development

Summary of Business

- Largest property company in Europe with portfolio of £8bn.
- Activities in London include flexible leasing, property outsourcing.
- Ordinary shares listed on London Stock Exchange.
- Share price = 1,400p.
- Financials for y/e 31st March 2005 (Land Securities Group):
    - Turnover = £1.6bn (£1.3bn, 2004)
    - Pre tax profit = £(155)m (£373m, 2004)
    - Net assets = £6.6bn (£6bn, 2004)
    - Long term loans of £2.9bn (£2bn, 2004)

Date of Interest June 2003

Summary of Proposal

- Would like to undertake a desktop study of the sites potential in the context of a wider brief on all the markets.
- Would like to work from the conclusions of the Saphir report, providing the lynch pin to a development partnership across all the market sites, with a view to rationalising the number of sites and the way in which they are operated, to release surplus land for development.
- Site may be best used as residential accommodation or hotel. Limited potential for offices and retail.

Other

Advantages identified by Land Securities of a partnership with Authority include:

- Diverse range of in house skills
- Committed to longer term projects
- Financial strength
- Good relationships with public sector authorities

Disadvantages includes:

- Site may not generate sufficient critical mass to make it an attractive mixed use proposition.
- Location is no ideal.

Auditors = PwC

Interest expressed by... **Parkview International London PLC**

On behalf of... Parkview International London PLC

Summary of Business

- Large unquoted company.
- Public limited with share capital.
- Provide property development and investment management services.
- Parent company = Festival Investments Ltd.
- Financials for y/e 31st March 04:
    - Turnover = £4m (£2,5m, 2003)
    - Pre tax profit = £260k (£262k, 2003)
    - Net assets = £1.5m (£4m, 2003)
    - Long term liabilities = £0 (£5.9m, 2003)

Date of Interest

May 2005

Summary of Proposal

Expression of interest to maximise the potential of the property both economically and aesthetically in combination with the Battersea Power Station master plan.

Other

Developers of Battersea Power Station, which is their registered address.

[redacted]

On behalf of...

An un-named major national development company

Summary of Business

PDA = Architects, linking needs of private and government organisations to the interests of individuals in an overall environmental context.

No financial information available, although website suggests that fees are often donated to charity.

Date of Interest

January 2005

Summary of Proposal

Would like to carry out consultation exercise relating to the East Battersea area, including NCGM.

Other

Wandsworth Economic Development Office do not take schemes by this partnership very seriously. They are not on their list of approved architects.

Interest expressed by...

St Modwen Properties PLC

On behalf of...

St Modwen Properties PLC

Summary of Business

- Ordinary shares listed on London Stock Exchange.
- Share price = 442p, P/E ration = 17.74.
- Engaged in property investment and development.
- Specialisms include town centre regeneration, partnering industry in its restructuring, brownfield land renewal and heritage restoration.
- Financials for y/e 30th November 04:
  - Turnover = £117m (£123m, 2003)
  - Pre tax profit = £40.3m (£30.5m, 2003)
  - Net assets = £267m (£223m, 2003)
  - Long term liabilities = £239m (£134m , 2003)

Date of Interest

July 2003

Summary of Proposal

Expression of interest only:

- Working on 'add on' elements for the market
- Working on ideas for a structure to suit the legal framework.

Interest expressed by... CB Richard Ellis Ltd

On behalf of... Taylor Woodrow PLC

Summary of Business

- Ordinary shares quoted on the London Stock Exchange.
- Share price = 331p, P/E ration = 7.14.
- Engaged in house building, general construction and investment in domestic and commercial properties.
- Financials for y/e 31st December 04:
  - Turnover = £3.4bn (£2.7bn, 2003)
  - Pre tax profit = £390m (£301m, 2003)
  - Net assets = £1.3bn (£1.2bn, 2003)
  - Long term loans = £699m (£845m, 2003)

Date of Interest September 2003

Summary of Proposal Expression of interest only.

Interest expressed by... CB Richard Ellis Ltd

On behalf of... The Berkeley Group

Summary of Business

- Ordinary shares listed on London Stock Exchange.
- Share price = 904p, P/E ratio = 7.5.
- Leader in urban regeneration, 95% of work on brownfield sites.
- Financials for y/e 30th April 2004:
  - Turnover = £1.3bn (£1.2bn, 2003)
  - Pre tax profit = £230m (£221m, 2003)
  - Net assets = £1.1bn (£1.1bn, 2003)
  - Long term loans = £85m (£222m, 2003)

Date of Interest September 2003

Summary of Proposal Expression of interest only, subsequently withdrawn, but with some ongoing contact.

Other Auditors = PwC

Interest expressed by... Urban Catalyst Ltd

On behalf of... Urban Catalyst Ltd

Summary of Business

- "Bridging the gap between the public and private sectors in the economic and physical regeneration of our towns and cities".
- Small unquoted company filing modified balance sheet only.
- Financials for y/e 31st March 2003:
  - Turnover = £8k (£54k, 2002)
  - Pre tax profit = £(315)k (£(208)k, 2002)
  - Net assets = £168k (£(265)k, 2002)

Date of Interest September 2003

Summary of Proposal Expression of interest only (although further details provided to Authority which we have not received)

Other Joint venture partners for previous projects include:

- Carillion PLC
- London Borough of Southwark
- Autograph
- Y2K Properties

Expression of Interest to provide consultancy services:

[redacted]

On behalf of... Aucxis Trading Solutions

Summary of Business

- Specialists in streamlining the trading and preservation processes of perishable goods.
- No financial information available.

Date of Interest July 2005

Summary of Proposal

- Interested in undertaking a specialist consultancy role as part of current/future studies.
- Interested in competing for any system required at the market for electronic sales.