Channel Islands Property Fund

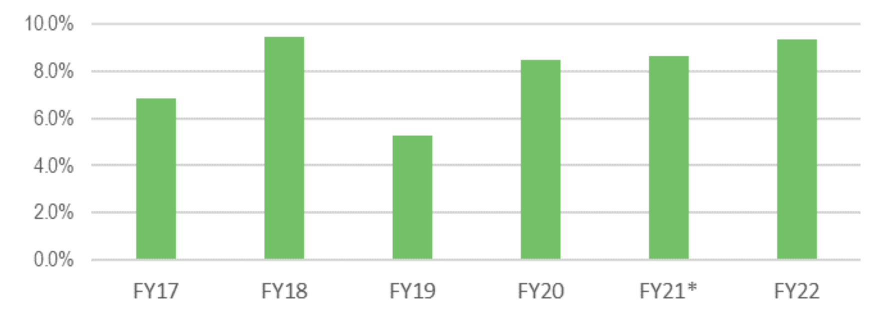
Sound income stream

Investment companies
Real estate

12 April 2023

Channel Islands Property Fund (CIPF) has proved to be a resilient investment since its launch in 2010 and remains an attractive income-generating fund with a 6.6% dividend yield. The markets it operates in, the Channel Islands and the Isle of Man, are withstanding current uncertainties over a potential recession and increasing interest rates relatively well compared to mainland UK in terms of property valuation. Nevertheless, CIPF management entered into two derivative agreements in FY22 to hedge its interest expenses, which resulted in a significant profit from the valuation of these instruments.

CIPF exhibits stable NAV total return



Source: Channel Islands Property Fund, Edison Investment Research. Note: *11-month period.

Attractions of investing in Channel Islands property

An investment in Channel Islands property is attractive for several reasons. Firstly, investment assets on the islands have defensive qualities, which include longer than average leases versus similar assets on the mainland, and the occupiers tend to be resilient finance industry companies with strong covenants. Secondly, during the pandemic, the strength of these covenants was validated with CIPF collecting 100% of anticipated rents. Lastly, yields tend to be higher than in comparable regional UK markets (at c 6% compared to 5.0–5.5%), offering scope for Channel Islands' yields to trend closer to regional levels and suggesting potential for capital uplift. This has seen the pool of global investors widen in recent years.

Income generating investment

The predictable nature of the rental income stream, paired with the stability of the Channel Islands property market, make CIPF a very attractive vehicle for investors looking for regular income. It distributes most of its income through quarterly dividends, with 6.6p per share distributed annually since 2017, which implies a 6.6% dividend yield on the current share price. The CIPF dividend yield is currently in line with the average yield of comparable companies, although this partially stems from widening discounts across the industry (while CIPF trades close to par). As the property valuations in the Channel Islands are relatively stable compared to mainland UK, CIPF's NAV return tends to be close to its dividend yield (8.0% pa over the five-year period to 31 December 2022).

NOT INTENDED FOR PERSONS IN THE EEA

Price		**100p**
Market cap		**£159.9m**
NAV*		**£154.3m**
NAV per share*		96.5p
Premium to NAV		3.6%

*Including income. As at 31 December 2022.

Yield		6.6%
Ordinary shares in issue		159.9m
Code/ISIN		CIP/GG00B62DS151
Primary exchange		TISE
AIC sector		Property Direct – UK
52-week high/low	103.5p	100.0p
NAV* high/low	99.7p	96.5p

*Including income.

Loan to value*	45.5%

*As at 31 December 2022.

Fund objective

Channel Islands Property Fund was established with the objective of offering an investment opportunity that provides shareholders with a total return from a combination of quarterly dividends and capital growth through the acquisition and active asset management of high-quality office properties in the Channel Islands and the Isle of Man.

Bull points

- Properties are mainly multi-let to blue-chip clients. The WAULT is long at 11.6 years as at 30 September 2022.
- Dividend yield of 6.6%.
- The Channel Islands and the Isle of Man have proved very attractive markets during lockdowns.

Bear points

- Core markets are capacity constrained.
- Low stock liquidity.
- NAV growth (excluding dividends) has been modest.

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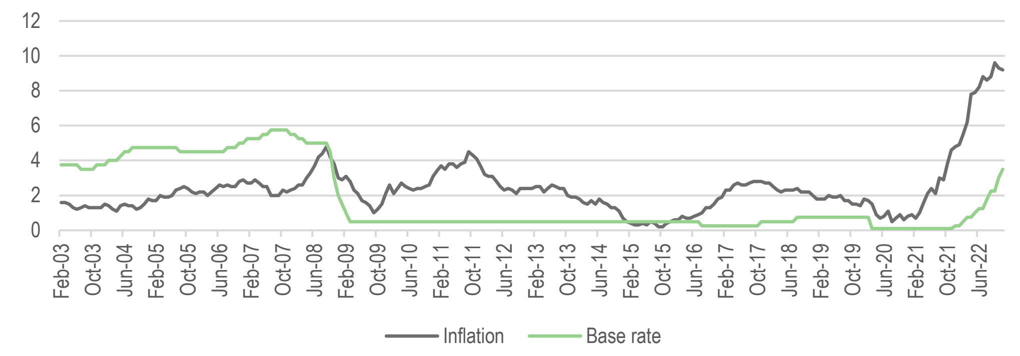
Edison profile page

Channel Islands Property Fund is a research client of Edison Investment Research Limited

Market outlook: Withstanding the turmoil

The Channel Islands and Isle of Man property markets are characterised by low supply of new office space, short commuting times and high demand. Despite increasing interest rates, property valuations in the Channel Islands remained relatively stable in 2022 (as highlighted by only a 3% reduction in the value of CIPF's property portfolio in FY22, as at 30 September 2022). Having said that, the Bank of England and the Federal Reserve in the United States expect interest rates to peak in 2023 at c 0.5pp higher than current rates. Short commuting times on the islands provide less incentive for employees to pursue work-from-home arrangements and therefore offices on the islands remain occupied. It is worth noting that the Channel Islands market withstood the COVID-19 pandemic well, with a limited number of cases and little disruption to regular operations, as highlighted by CIPF's 100% rent collection during lockdowns.

Exhibit 1: UK headline inflation* and base rate over the last 20 years



Source: Office for National Statistics, Bank of England. Note: *Defined as Consumer Prices Index with housing.

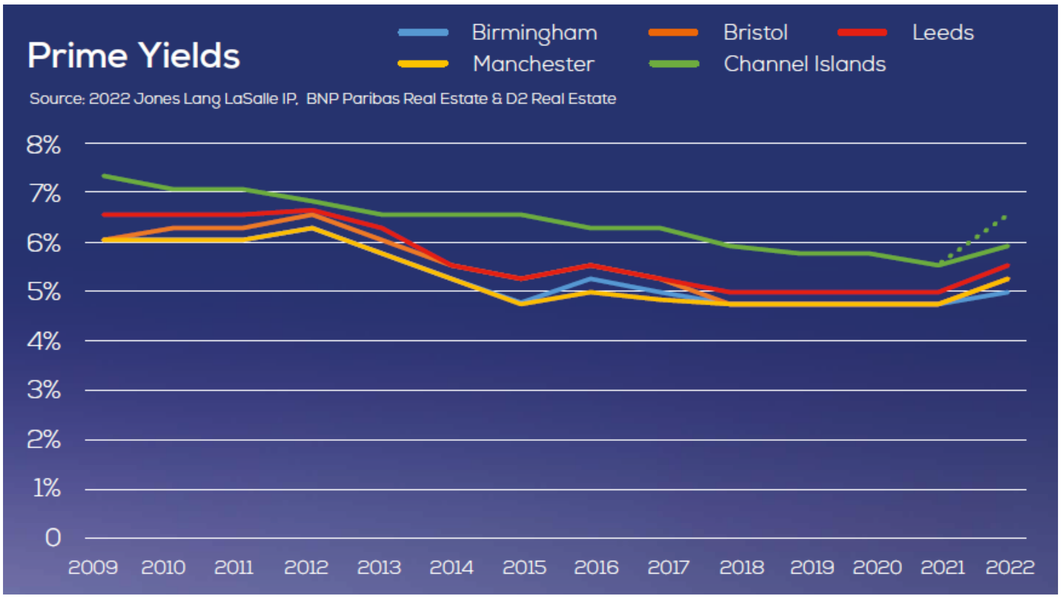
Structural changes prompted by the pandemic

D2 Real Estate (D2RE, which also acts as CIPF's property manager) expects the Channel Islands market conditions to improve relatively quickly as interest rates are forecast to start to fall towards the latter part of the year. It also sees investors in mainland UK adopting a 'wait and see' approach, given the structural reshaping of the industry prompted by the increasing popularity of hybrid work arrangements – a factor far less relevant in the Channel Islands though. According to the National Bureau of Economic Research, there is a clear correlation between the popularity of working from home and average daily commuting time (the more time it takes to get to the office, the more employees are willing to work from home). This implies that office working is more popular in the Channel Islands due to its short commuting times. On top of that, the property stock in the Channel Islands is far more limited than in the UK, which means the right opportunity still attracts an active pool of buyers.

Supply constraints make the Channel Islands attractive

An important advantage of the Channel Islands market is the limited number of new properties being developed, due to its geographical limitations. Naturally, this translates into higher competition for quality assets and lower tenant turnover, aiding market stability. Having said that, several larger investments were brought to the market in the second half of 2022, allowing the current, more uncertain market conditions to be reflected in property transactions, as investors tend to compare returns against other jurisdictions. This is visible in the higher yields reported on new leases with a tenure of 15+ years (ie for new properties), as presented in Exhibit 2 below.

Exhibit 2: Prime yields



Source: D2 Real Estate. Note: Given limited evidence in Q422, the yield data is mainly 'sentiment based'. The yield spread for the Channel Islands, as indicated by the green dotted line, shows the potential range between brand new, 15+ year lease versus five-year and weighted average unexpired lease term (WAULT) sub 10 years.

Jersey

At the end of 2021, Jersey's occupational market comprised c 3m sq ft office space, of which CIPF had a c 5.5% market share. According to D2RE, as of February 2023, there are 214k sq ft of office space under construction:

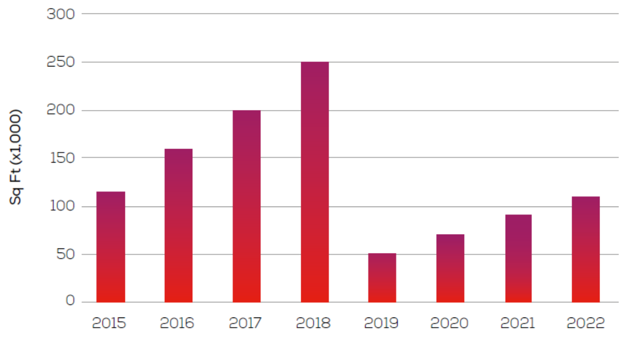
- Cyril Le Marquand House, developed by the Government of Jersey, will comprise 100k sq ft;
- 8 Esplanade, developed by Dandara, will comprise 50k sq ft; and
- International Finance Centre 6 is due to complete in Q423 with 64k sq ft. The majority (89%) of the space has been pre-let to Aztec.

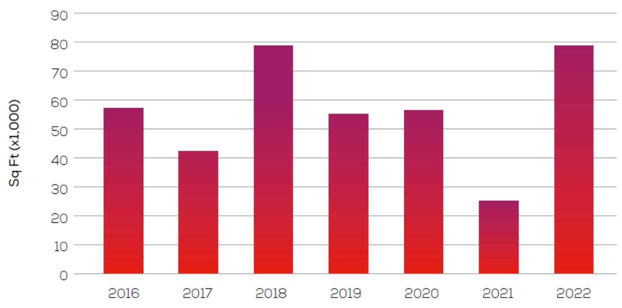
The take-up in Jersey decreased visibly in 2019 and has been gradually increasing since then. According to D2RE, the lower take-up figures reflect a lack of stock rather than a lack of demand. The vacancy rate in St Helier is around 8%, but, according to D2RE, much of the vacant space is in secondary locations and/or buildings not fit for purpose and the vacancy rate on the Esplanade (the financial centre of the island) is only 2%. These figures compare to CIPF's 4% vacancy rate across the whole portfolio, across all locations.

The recent activity in Jersey has been around second-generation buildings (ie built in the 2000s) in prime locations of St Helier. This is likely due to the limited amount of new buildings entering the market and wide rent differentials, which recently stood at £40/sq ft in new buildings and £28–30/sq ft in second-generation buildings. As a result, some upward pressure on second-generation rents is seen; as an example, CIPF's Liberation House had average rent of £28.5/sq ft pre-pandemic, while latest lettings and re-gears reached £32/sq ft.

Exhibit 3: Office take-up by year

St Helier (Jersey)	St Peter Port (Guernsey)





Source: D2 Real Estate. Note: Excludes lease completions that were the result of pre-lets, which have been allocated to the year that the agreement to lease was signed.

Guernsey

At the end of 2021, the Guernsey occupational market comprised c 2m sq ft office space, of which CIPF had a c 13.7% market share. Only one building is currently being developed in St Peter Port (Plaza House, due for completion in Q324), comprising 60k sq ft, of which 60% has been pre-let. This pre-letting has driven the highest take-up in Guernsey since 2018, at c 80k sq ft. The overall vacancy rate in Guernsey stood at 9.4% in 2022, down from 11.0% in 2021, but the grade A vacancy rate is as low as 2.9%. Even that is an inflated number due to the remainder of Plaza House being on offer (2021: 1.7%).

Isle of Man

The Isle of Man is the smallest property market CIPF operates in, being roughly one-third of the size of Jersey and half the size of Guernsey. The location is supply constrained and, according to CIPF, no new investments entered the market during FY22. Simultaneously, yields on the Isle of Man are visibly higher than on the Channel Islands (see Exhibit 4), which we believe may stem from lower tenant and investor interest. Having said that, the largest office building in Douglas (Douglas Bay House) completed a lease re-gear during the last year.

The investment manager: Ravenscroft Specialist Fund Management

The manager's view

Commercial real estate tends to be adversely affected as economic conditions worsen, driven by a combination of yields available in the gilt and bond market plus a discount for liquidity – it takes longer to sell physical real estate than bonds. Recent movements in the share prices of listed real estate investment trusts (REITs) suggest a fall in pricing of property over the next 12 months at least.

According to CIPF's management, the fund will undoubtedly be affected by changing conditions in the wider market, however the underlying portfolio has been constructed to be defensive in times of turbulence, with high-quality assets in a market lacking oversupply of stock, let on long leases to good tenants, with 100% rent collection throughout the pandemic. In contrast to many UK regional cities, offices in the Crown Dependencies are operating with a high level of staff occupancy, partly because of short commuting distances on the islands.

Crucially, rental growth in St Helier and St Peter Port is still in evidence and this is one of the key drivers for value in a real estate portfolio. Another value driver is tenant demand, and the manager has seen new lettings in the portfolio over the last two quarters, in addition to take up in other new-build properties in the Crown Dependencies.

Portfolio positioning

CIPF's portfolio consists of 12 properties: five in Guernsey, four in Jersey and three in the Isle of Man. All are A-grade properties with long-term leases, which collectively had a WAULT to expiry of 11.6 years at 30 September 2022 and as high as 23 years at 17a–18 Esplanade (with the earliest possible enactment of break clause in 2024). The property mix remains stable, with the latest addition to the portfolio being 18–22 Grenville Street, acquired in September 2020. This long-term visibility gives investors confidence that the fund will be able to pay its expected future dividends, which is one of CIPF's major attractions.

Exhibit 4: Portfolio by location, value and area as at 30 September 2022

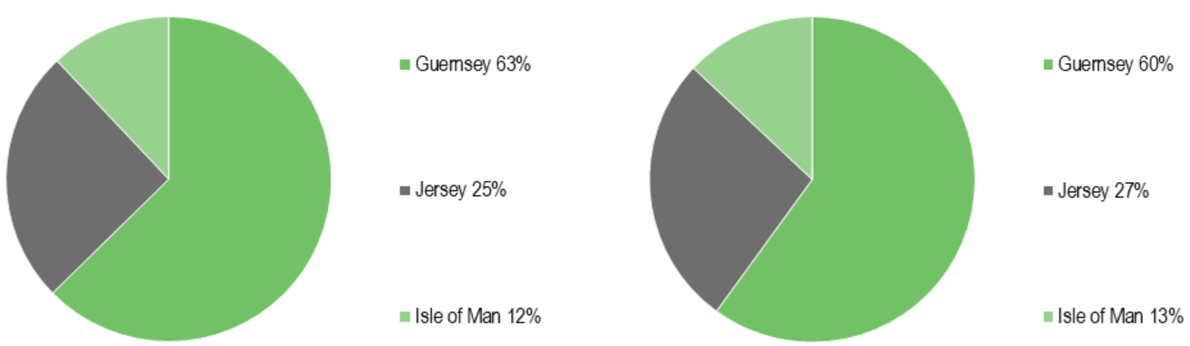
Property	Location	Contracted rent (£m)	Gross yield (%)	Area (sq ft)	% of total space	WAULT to expiry (years)	Purchased
Regency Court	Guernsey	2.7	7.0%	59,603	11.5%	6.8	Nov-10
Glategny Court	Guernsey	2.9	6.5%	61,706	11.9%	13.2	Aug-14
Royal Chambers & The Rotunda	Guernsey	3.4	7.3%	73,973	14.3%	13.1	Sep-17
Royal Bank Place	Guernsey	1.3	4.8%	42,787	8.3%	10.2	Jun-19
Oak House	Guernsey	0.5	6.8%	14,782	2.9%	12.3	Jul-20
		10.8	**6.6%**	**252,851**	**48.8%**	**11.3**	
17a–18 Esplanade	Jersey	0.9	7.4%	29,241	5.6%	23.1	Jul-13
Liberation House	Jersey	2.1	7.8%	62,733	12.1%	7.1	Sep-16
Windward House	Jersey	0.8	8.1%	24,081	4.6%	5.5	Sep-16
18–22 Grenville Street	Jersey	1.2	6.3%	50,141	9.7%	12.5	Sep-20
		4.9	**7.3%**	**166,196**	**32.1%**	**11.0**	
Fort Anne	Isle of Man	1.1	8.3%	45,989	8.9%	14.9	Aug-16
Vicarage House	Isle of Man	0.8	7.1%	30,000	5.8%	9.6	May-17
First Names House	Isle of Man	0.5	7.8%	23,462	4.5%	15.7	Jun-17
		2.5	**7.7%**	**99,451**	**19.2%**	**13.5**	
Total		**18.2**	**6.9%**	**518,498**	**100.0%**	**11.6**	

Source: Channel Islands Property Fund, Edison Investment Research

Two-thirds of CIPF's portfolio (value-wise) is located in Guernsey, a quarter in Jersey and the remaining 12% on the Isle of Man (see Exhibit 5). The yields earned on Jersey and Isle of Man are visibly higher than in Guernsey, which translates into their higher share in overall contracted rent compared to their share in the total property portfolio value.

Exhibit 5: Capital value and contracted income by location, at 31 December 2022

Capital value by property as a percentage of portfolio | **Contracted rent by property as a percentage of portfolio**



Source: Channel Islands Property Fund, Edison Investment Research

The annual rental income of CIPF portfolio was £18.3m as at 31 December 2022 (compared to £17.6m in July 2021). The three largest properties (in terms of value, data as at 30 September

2022) are in Guernsey and generate 49% of contracted rent. All are multi-tenant offices, rented predominantly to financial institutions:

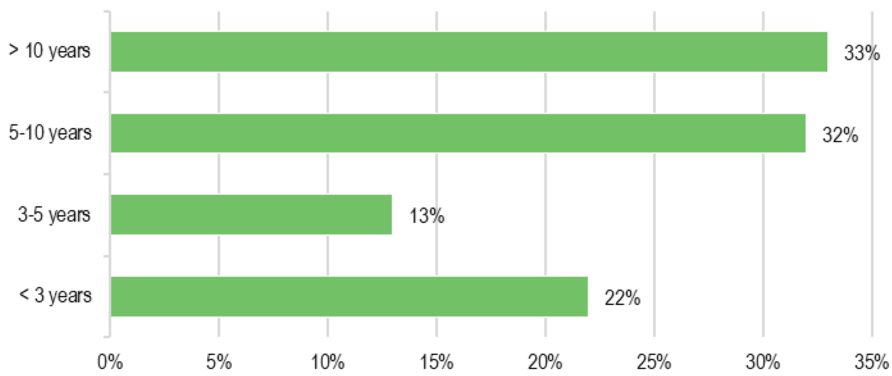
- **Royal Chambers & The Rotunda** – the property is situated in St Peter Port, directly opposite the harbour, in Guernsey's finance district. It is let to four tenants: Mourant (39.3% of contracted rent), EY (32.3%), Apex (18.0%) and Terra Firma (10.4%).
- **Glategny Court** – the property is also located in St Peter Port, overlooking the Queen Elizabeth II Marina. It is sublet broadly evenly among four tenants: KPMG (26.5%), Collas Crill (26.4%), Guernsey Financial Services Commission (23.8%) and Investec (23.2%).
- **Regency Court** – the building neighbours Glategny Court in St Peter Port and shares the view over the marina. More than half (54.8%) of its contracted rent comes from Bank of Butterfield, with the remaining three tenants being Schroders (16.8%), Deloitte (14.4%) and Alter Domus (14.1%)

The single largest tenant exposure in CIPF's portfolio is Mourant, representing 14% of CIPF's contracted rent. It rents roughly half of the abovementioned Royal Chambers and the entire office space in 18–22 Grenville Street in Jersey. Mourant is one of the largest offshore law firms, with offices in the British Virgin Islands, Cayman Islands, Channel Islands, Hong Kong and the UK. None of the other 26 tenants represent more than 10% of the contracted rent. The tenants in the portfolio are mostly blue-chip financial and legal firms and, as such, can be considered good quality.

Six of CIPF's 12 portfolio properties are let to single tenants. These represent 29% of the portfolio in terms of property value and 28% in terms of generated rent as at 30 September 2022.

CIPF's portfolio is almost fully let, with a vacancy rate of 3.7% at 30 September 2022 (down from 4.8% a year earlier), which compares to, for example, a 7.5% vacancy rate at CLS Holdings. A third of CIPF's contracted rent has an earliest termination date after more than 10 years, while 22% has a termination date below three years. However, we do not see the shorter-term agreements as a risk, considering the lack of new space coming to the market, and the attractiveness of the locations, implying a steady stream of interested occupiers. We believe that five- to six-year lease terms are more common in the UK office space, compared to longer durations common in the Channel Islands, as well as in the CIPF portfolio. These characteristics highlight the attractiveness of the Channel Islands market.

Exhibit 6: Portfolio by earliest termination date (% of contracted rent) at 30 September 2022

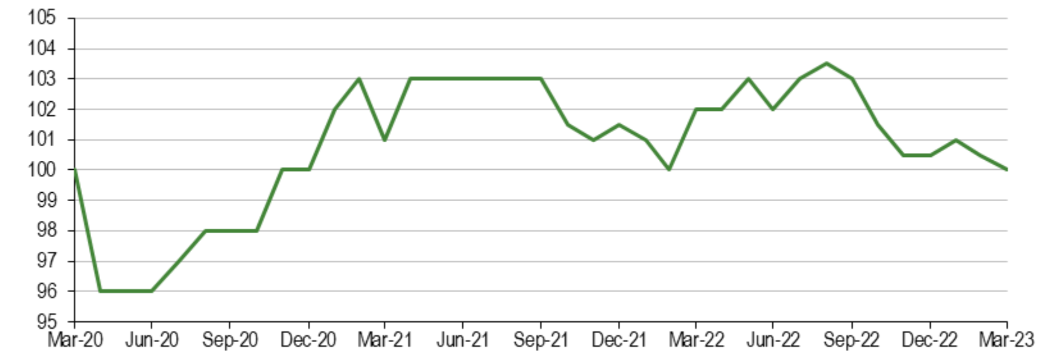


Source: Channel Islands Property Fund

Performance: Remarkably stable over the long term

CIPF listed in 2010 at 100p and has remained broadly at that level for over 12 years. It briefly dipped to 96p during the initial outbreak of the COVID-19 pandemic and related turmoil in financial markets, but rebounded subsequently to the current 100p. We believe this stability is driven primarily by the fund paying out most of its earnings as dividends; the trade-off for growth in the underlying assets is a dependable dividend stream.

Exhibit 7: CIPF's share price performance over three years

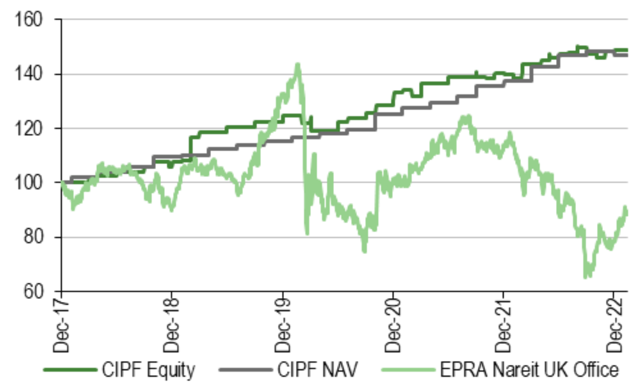


Source: Refinitiv, Edison Investment Research

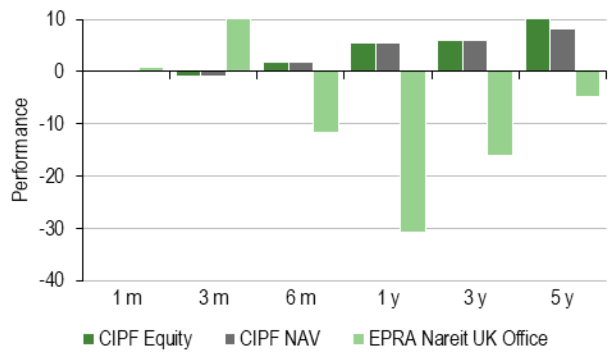
The defensiveness of CIPF's stock has proved beneficial for investors in the bear market. CIPF shares did not follow the recent sell-off, as seen in the broad index (see Exhibit 8), leading to its significant relative outperformance against the index. CIPF's average annual NAV total return to 31 December 2022 is 8% pa over the last five years, compared to a 5% decrease pa of the EPRA Nareit UK office index. We believe that CIPF's defensiveness stems, at least partially, from low share liquidity. Nevertheless, looking at the period before the sell-off (the five-year period ending 31 December 2021), CIPF still visibly outperformed the broader UK office market, with a 8.0% NAV total return per annum, compared to 6.4% for the index.

Exhibit 8: Investment trust performance to 31 December 2022

Price, NAV and benchmark total return performance, five-years rebased



Price, NAV and benchmark total return performance (%)

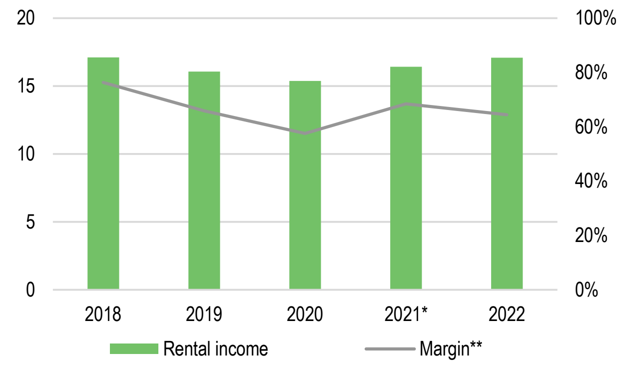


Source: Refinitiv, The International Stock Exchange, Edison Investment Research. Note: Three- and five-year performance figures annualised.

CIPF's rental income amounted to £17.1m in FY22, compared to £16.4m in FY21, which was an 11-month period due to a reporting period change. It is important to note that CIPF collected 100% of contracted rent in FY20 during the period of lockdowns, highlighting the strength of its tenants. The property costs (utilities, maintenance, etc) are passed on to tenants through a service charge collected quarterly in advance, based on the budgeted amount for each year, while CIPF needs to cover costs related to the vacant space on its own. In FY22, CIPF incurred £4.2m in service charge expenses (up 13% y-o-y) of which only £0.3m was non-recoverable (though up 10% y-o-y). The remaining operating expenses comprise management costs (FY22: £1.7m) as well as other expenses (including administration, legal and remuneration, among others) of £1.6m in FY22. The slight cost inflation resulted in a decline in operating margin to 64% of total income, from 69% in FY21.

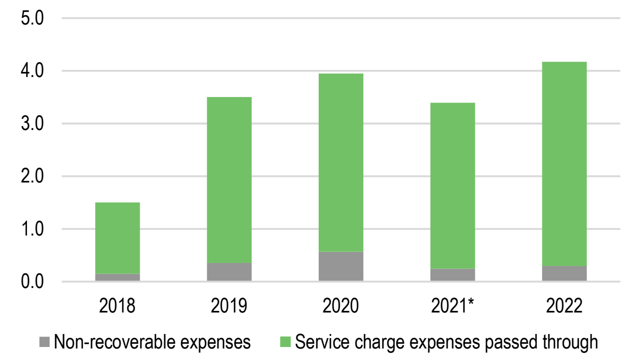
CIPF's net income for FY22 was £14.5m, up 43% y-o-y on an annualised basis. The year-on-year change (given broadly stable operating income) stemmed from revaluations. The £8.3m downward revaluation of investments was fully offset by a £14.2m profit recognised on revaluation of derivative instruments (see more in the Gearing section below). We calculate net income, excluding the impact of derivatives revaluation, stood at £0.3m (FY21: £9.3m).

Exhibit 9: CIPF's rental income



Source: Channel Islands Property Fund, Edison Investment Research. Note: *11-month period. **Operating income margin excluding profit/loss on revaluation.

Exhibit 10: CIPF's maintenance costs



Source: Channel Islands Property Fund, Edison Investment Research. Note: *11-month period.

Peer group comparison

CIPF does not have any direct peers, but we list below a selection of REITs and funds that have similar characteristics, that is, they tend to hold office, commercial or retail property portfolios. CIPF's NAV performance ranks above the group average over the periods of one to five years to 31 December 2022. We note that CIPF's property portfolio is relatively stable valuation wise and did not follow the recent downward revaluation seen among peers. Similarly, it withstood the pandemic well compared to peers and was not subjected to subsequent rebound in valuations. We also note that the average share price discount to NAV widened recently among peers to 22% (compared to 10% in November 2021), most likely reflecting higher yield expectations of investors in the environment of higher interest rates. CIPF's dividend yield now stands at 6.6%, which is below the peer group average; however, we note that the average peer yield increased to 7.2% from 4.7% in November 2021.

Exhibit 11: Selected peer group at 12 April 2023*

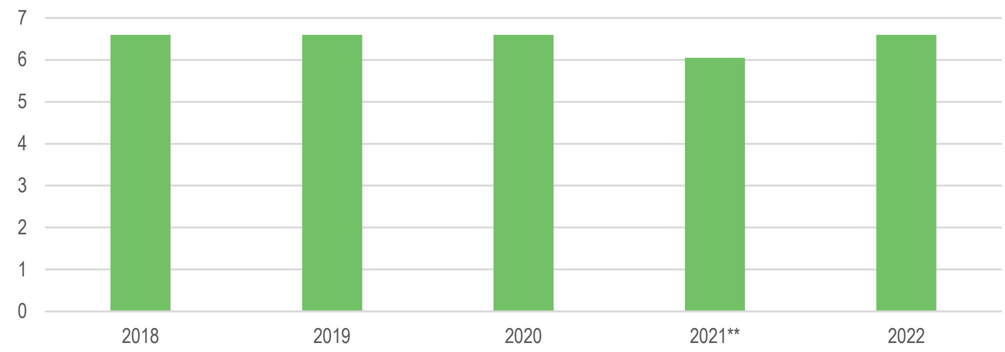
% unless stated	Market cap (£m)	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	Discount (ex-par)	Ongoing charge ex perf fee	Perf. fee	Net gearing (ex par)	Income-only yield (%)
Channel Islands Property	**159.9**	**5.6**	**19.1**	**48.4**	**3.6**	**2.3**	**No**	**171**	**6.6**
abrdn Property Income Trust	207.4	(13.7)	6.1	21.1	(34.4)	2.2	No	119	7.4
AEW UK REIT	152.1	(1.9)	36.2	57.4	(6.7)	4.6	No	107	8.3
Alternative Income REIT	54.2	2.5	6.4	19.7	(18.9)	2.0	No	151	8.5
Balanced Commercial Property	609.6	(9.4)	(0.8)	0.2	(26.4)	1.3	No	126	5.5
CT Property Trust	154.1	(18.8)	3.2	10.9	(29.7)	1.5	No	138	6.0
Custodian Property Income REIT	403.4	(8.1)	11.9	24.7	(7.0)	1.9	No	123	6.0
Ediston Property Investment Co	140.7	(5.9)	(6.2)	(6.9)	(17.3)	1.4	No	114	7.5
LXI REIT	1,731.6	5.8	35.4	70.2	(27.7)	0.9	No	100	6.2
Regional REIT	269.7	(21.2)	(21.9)	(3.6)	(25.5)	5.8	Yes	184	12.6
Schroder Real Estate Invest	226.5	(8.3)	12.0	12.1	(24.3)	2.2	No	145	6.4
Supermarket Income REIT	1,097.9	(14.5)	12.0	30.0	(2.4)	1.1	No	138	6.8
UK Commercial Property REIT	686.1	(18.3)	(1.3)	3.4	(33.0)	1.4	No	115	6.3
Value and Indexed Property Income	88.2	4.3	(1.5)	1.6	(29.7)	1.7	No	130	6.1
Peers' average	**447.8**	**(8.3)**	**7.0**	**18.5**	**(21.8)**	**2.1**	**-**	**130**	**7.2**
Rank	**9**	**2**	**3**	**3**	**1**	**3**	**-**	**2**	**7**

Source: Morningstar, Edison Investment Research. Note: *Performance at 31 December 2022 based on ex-par NAV. TR = total return. NAV TR is on a cumulative basis. Net gearing is total assets less cash and equivalents as a percentage of net assets. 100 = ungeared.

Quarterly dividends at 6.6% yield

We consider CIPF's regular dividends as one of the stock's most important features for investors. Since 2017, CIPF has distributed a dividend of 6.6p per share every year in equal quarterly instalments, which implies a 6.6% yield at the current share price. The dividends are paid in February, May, August and November. The company distributes most of its income through dividends, and the relation of dividend to net income stands at 89% on a three-year average. The last dividend payment was made on the last day of February (ex-dividend date was 6 February).

Exhibit 12: Dividend history, last five years* (DPS, p)

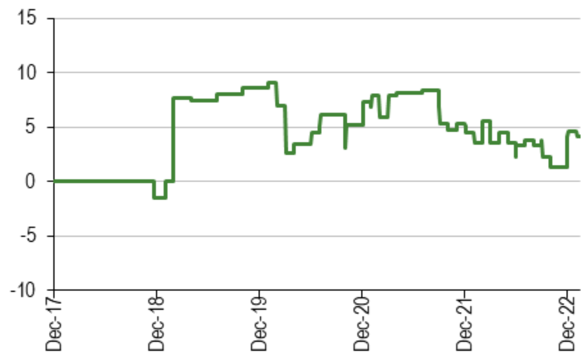


Source: Channel Islands Property Fund, Edison Investment Research. Note: *Dividends paid in a calendar year. **CIPF has changed its year-end and dividend distribution schedule, and the payment made in November 2021 was 1.10p from a two-month income, still implying a 6.6p DPS on a 12-month basis.

Trading close to par

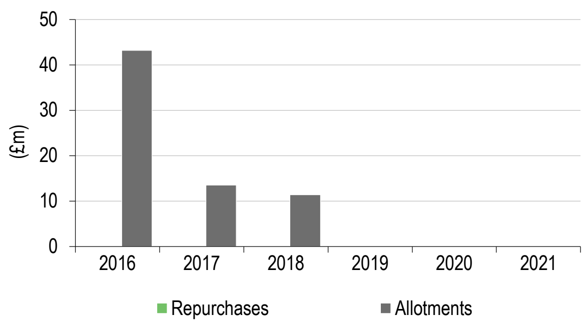
CIPF tends to trade at a slight premium to its NAV while its peers trade at a double-digit discount. We believe this is because its assets and tenants are high quality. Therefore, the rental income is very predictable and, even in the pandemic, CIPF collected all rent due in every quarter. It follows then that investors value the company on a dividend yield basis.

Exhibit 13: Share price discount to NAV



Source: Refinitiv, The International Stock Exchange, Edison Investment Research

Exhibit 14: Buybacks and issuance



Source: Morningstar, Edison Investment Research

Fund profile: A stable income vehicle

The company was established in 2010 with the objective of providing shareholders with a total return from a combination of capital growth and an appropriate dividend policy through the acquisition and active management of commercial property, predominantly in the Channel Islands.

CIPF distributes most of its income in the form of dividends, and its net asset value remains relatively stable over time.

The company was initially set up with a limited life, but at the 2018 AGM shareholders voted to extend the life of the company indefinitely, subject to a continuation vote every five years. The shareholders representing at least 15% of issued shares had the opportunity to request such a vote at the next AGM to be held on 2 March 2023; they did not exercise this and the next vote may be requested at the 2028 AGM.

The company's investments are not subject to any geographical or other limitations or restrictions, although its investment objective is to hold properties predominantly located in the Channel Islands. The company may invest directly or indirectly in commercial property including property development as long as no single investment is more than 25% of the portfolio. Investment in property related funds, derivatives and financial indices is also permitted. Leverage is targeted at 40–65% of total acquisition cost. Day-to-day management is delegated to Ravenscroft as the investment manager, and to D2RE as the property manager.

CIPF's approach to ESG

CIPF seeks to ensure that sustainability considerations are integrated into investment decisions and the ongoing management of the portfolio. CIPF promotes social responsibility, acting with integrity in governance and aiming to ensure that its actions fully take into account their effect on the environment, and it has developed its own ESG objectives, which are:

- to have a positive effect on the communities in which it operates;
- to be the landlord of choice based on its responsible, sustainable, ethical and transparent approach;
- to mitigate climate change; and
- to maintain ethics and integrity in its governance and dealings.

CIPF works collaboratively with its tenants, which have their own ESG agendas, to deliver results together. CIPF encourages green leases with all incoming tenants and is working on memoranda of understanding with existing tenants to develop deliverable initiatives in this area, which is of great importance to them as occupiers and for staff expectations and occupier experience.

CIPF as a company has a limited footprint, but it seeks to reduce travel with the use of video conference calls. The day-to-day management of its portfolio is undertaken by D2RE, and examples of how D2RE incorporates ESG include:

- delivering a 'local sourcing first' policy for all suppliers to ensure as much money and benefit is put back into the local economies as possible;
- all hard services maintenance contracts are to industry best standard SFG20. This proactive approach is claimed to be able to reduce consumption by up to 15% and reduce unplanned reactive visits;
- considering the lifecycle of mechanical and electrical assets when undertaking replacement projects. For example, a lift replacement project had a requirement for all new equipment to be 90% recyclable at end of life;
- embracing technological advances with replacement projects; and
- encouraging suppliers to incorporate ESG considerations into their project work. For example, this led to a generator being donated to a Ukrainian hospital.

According to CIPF, ESG issues are at the forefront of decision-making both for occupiers and investors. While valuers are not yet directed to explicitly consider ESG in deriving their opinion of property valuations, it is an inevitable factor in the future, with the possibility of 'green premia' and 'brown discounts' being applied to values. The manager actively monitors the market and acts in a timely fashion to ensure that buildings will be compliant with relevant legislation in the future. The States of Jersey has introduced energy performance certificates (EPCs), with standards expected to follow closely those that have been in place in the UK for many years. CIPF has already obtained EPCs for most of its properties, with good overall results.

Gearing: Hedging against interest rates

In FY22, CIPF amended its loan facility from Royal Bank of Scotland International (RBSI) to enlarge it to £125m (from £120m), of which £5m remained undrawn at 30 September 2022. The loan matures in June 2027 and bears a variable interest, which at 30 September 2022 was 5.50% (the current margin was not disclosed, while it was 2.39% at 30 September 2021). The commitment fee stands at 1.00% of the undrawn amount.

The loan has five covenants in place (see Exhibit 15), all of which were met as at 30 September 2022. Having said that, the increase in interest rates during the year (eg three-month sterling Libor increased from 0.08% on 30 September 2021 to 3.34% on 30 September 2022) translated into lower property valuations and in turn had a negative impact on the covenant ratios.

CIPF's current indebtedness implies a loan to value ratio (excluding lease incentives) of 49.3%, up from 47.9% at 30 September 2021. We calculate that to reach the 55% covenant threshold, CIPF's property portfolio would have to be revalued downwards by 11%. Considering that over the last year, which has seen a significant hike in interest rates, the portfolio was revalued down by only 3.1% and given current expectations of gradual policy easing, we see that level as relatively safe.

Exhibit 15: CIPF's covenants under loan facility

Covenant	Requirement	30 September 2022	30 September 2021	y-o-y
Loan to market value ratio (including lease incentives)	Must not exceed 55%	47.75%	46.29%	1.5pp
Loan to market value ratio (excluding lease incentives)	Must not exceed 55%	49.30%	47.89%	1.4pp
Projected interest cover ratio	Must be in excess of 225%	402.11%	712.42%	(310.3pp)
Historical interest cover ratio	Must be in excess of 225%	442.73%	541.70%	(99.0pp)
Projected debt to rent cover	Must not exceed 900%	648.69%	652.22%	(3.5pp)

Source: Channel Islands Property Fund

Additionally, CIPF actively manages its interest rate exposure and entered into two derivatives agreements over the last financial year. The derivative arrangements were signed with NatWest Markets and cover £90m out of CIPF's overall £120m loan exposure. CIPF has an interest rate swap in place for £45m (carried out at 1.67%) and an interest rate cap with a strike rate of 1% on the other £45m. During the year, the derivative instruments were revalued by £14.2m, which significantly improved CIPF's bottom line.

Exhibit 16: CIPF's derivative instruments

Instrument	Notional amount	FY22 revaluation
Interest rate swap	£45m	£6.3m
Interest rate cap	£45m	£7.9m
Total		£14.2m

Source: Channel Islands Property Fund

Fees and charges: No incentive fees

CIPF's ongoing charge amounted to 2.10% of average NAV in FY22 (FY21: 1.97%). The charge includes the management fee paid to the investment manager (0.6% of the gross asset value of the company), as well as other ongoing costs of administration, regulators and auditors, among others. The manager does not charge any performance fees and property management costs are mostly covered by the service charge.

Very simple capital structure

CIPF was established in 2010 as a closed-ended collective investment scheme authorised by the Guernsey Financial Services Commission. It has a single class of share, of which there are now 159.9m shares in issue. Its biggest shareholder is Huntress (CI) Nominees, which holds 87% of the issued share capital. Huntress (CI) Nominees is the vehicle through which the clients of Ravenscroft (CI) Limited hold stock in CIPF. We understand that within Huntress there are 736 shareholders, none of which holds more than 10% of the share capital.

Exhibit 17: Shareholders at 23 February 2023

Name	Holding (m)	%
Huntress (CI) Nominees	139.0	87.0%
State Street Nominees	8.0	5.0%
Pershing Nominees	3.1	2.0%
Security Services Nominees	3.0	1.9%
BNY Nominees	2.3	1.4%
SBS Nominees	1.5	0.9%
Vestra Wealth (Jersey)	1.3	0.8%
Other	1.7	1.0%
Total	**159.9**	**100%**

Source: Channel Islands Property Fund

The board

The board of CIPF consists of the chairperson and three directors, all of whom are considered independent. For more details, see our initiation report from November 2021.

Exhibit 18: Channel Islands Property Fund's board of directors

Board member	Date of appointment	Remuneration in FY22 (£)	Shareholdings at end-FY22
Shelagh Mason	14 October 2010	57,000	100,000
Steve Le Page	1 April 2017	42,000	100,000
Paul Le Marquand	1 December 2018	35,760	-
Paul Turner	1 April 2019	35,760	20,000

Source: Channel Islands Property Fund

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