

15. VALUATION OF INVESTMENT PROPERTY

	Deemed cost £000	Revaluation on deemed cost £000	Valuation £000
Freehold stores			
At 31 March 2017	583,297	527,613	1,110,910
Transfer from investment property under construction	11,763	(2,053)	9,710
Movement in year	7,780	73,452	81,232
At 31 March 2018	602,840	599,012	1,201,852
Leasehold stores			
At 31 March 2017	16,210	27,270	43,480
Movement in year	367	(557)	(190)
At 31 March 2018	16,577	26,713	43,290
Total of open stores			
At 31 March 2017	599,507	554,883	1,154,390
Transfer from investment property under construction	11,763	(2,053)	9,710
Movement in year	8,147	72,895	81,042
At 31 March 2018	619,417	625,725	1,245,142
Investment property under construction			
At 31 March 2017	45,477	(9,362)	36,115
Transfer to investment property	(11,763)	2,053	(9,710)
Movement in year	33,012	(1,260)	31,752
At 31 March 2018	66,726	(8,569)	58,157
Valuation of all investment property			
At 31 March 2017	644,984	545,521	1,190,505
Movement in year	41,159	71,635	112,794
At 31 March 2018	686,143	617,156	1,303,299

The Group has classified the fair value investment property and the investment property under construction within Level 3 of the fair value hierarchy. There has been no transfer to or from Level 3 in the year.

The wholly owned freehold and leasehold investment properties have been valued at 31 March 2018 by external valuers, Cushman & Wakefield (“C&W”). The valuation has been carried out in accordance with the RICS Valuation – Global Standards, published by The Royal Institution of Chartered Surveyors (“the Red Book”). The valuation of each of the investment properties and the investment properties under construction has been prepared on the basis of either Fair Value or Fair Value as a fully equipped operational entity, having regard to trading potential, as appropriate.

The valuation has been provided for accounts purposes and as such, is a Regulated Purpose Valuation as defined in the Red Book. In compliance with the disclosure requirements of the Red Book, C&W have confirmed that:

- > one of the members of the RICS who has been a signatory to the valuations provided to the Group for the same purposes as this valuation, has done so since September 2004. This is the third occasion on which the other member has been a signatory;
- > C&W have been carrying out this annual valuation for the same purposes as this valuation on behalf of the Group since September 2004;
- > C&W do not provide other significant professional or agency services to the Group;
- > in relation to the preceding financial year of C&W, the proportion of the total fees payable by the Group to the total fee income of the firm is less than 5%; and
- > the fee payable to C&W is a fixed amount per store, and is not contingent on the appraised value.

Market uncertainty

C&W's valuation report comments on valuation uncertainty resulting from low liquidity in the market for self storage property. C&W note that in the UK since Q1 2015 there have only been thirteen transactions involving multiple assets and ten single asset transactions. C&W state that due to the lack of comparable market information in the self storage sector, there is greater uncertainty attached to their opinion of value than would be anticipated during more active market conditions.

Portfolio Premium

C&W's valuation report further confirms that the properties have been valued individually but that if the portfolio was to be sold as a single lot or in selected groups of properties, the total value could differ significantly. C&W state that in current market conditions they are of the view that there could be a material portfolio premium.

Notes to the Financial Statements (continued)

Year ended 31 March 2018

15. VALUATION OF INVESTMENT PROPERTY (continued)

Assumptions

- Net operating income is based on projected revenue received less projected operating costs together with a central administration charge of 6% of the estimated annual revenue subject to a cap and a collar. The initial net operating income is calculated by estimating the net operating income in the first 12 months following the valuation date.
- The net operating income in future years is calculated assuming either straight-line absorption from day one actual occupancy or variable absorption over years one to four of the cash flow period, to an estimated stabilised/mature occupancy level. In the valuation the assumed stabilised occupancy level for the 74 trading stores (both freeholds and leaseholds) open at 31 March 2018 averages 83.6% (31 March 2017: 82.8%). The projected revenues and costs have been adjusted for estimated cost inflation and revenue growth. The average time assumed for the 74 stores to trade at their maturity levels is 16 months (31 March 2017: 22 months).
- The capitalisation rates applied to existing and future net cash flow have been estimated by reference to underlying yields for industrial and retail warehouse property, yields for other trading property types such as student housing and hotels, bank base rates, ten-year money rates, inflation and the available evidence of transactions in the sector. The valuation included in the accounts assumes rental growth in future periods. If an assumption of no rental growth is applied to the external valuation, the net initial yield pre-administration expenses for the 74 stores is 6.5% (31 March 2017: 6.5%) rising to a stabilised net yield pre-administration expenses of 6.9% (31 March 2017: 7.2%). The weighted average exit capitalisation rate adopted (for both freeholds and leaseholds) is 6.3% (31 March 2017: 6.6%).
- The future net cash flow projections (including revenue growth and cost inflation) have been discounted at a rate that reflects the risk associated with each asset. The weighted average annual discount rate adopted (for both freeholds and leaseholds) is 9.4% (31 March 2017: 9.7%).
- Purchaser's costs in the range of circa 6.1% to circa 6.8% (see below) have been assumed initially, reflecting the progressive SLDT rates brought into force in March 2016 and sale plus purchaser's costs totalling circa 7.1% to 7.8% are assumed on the notional sales in the tenth year in relation to the freehold and long leasehold stores.

Short leasehold

The same methodology has been used as for freeholds, except that no sale of the assets in the tenth year is assumed but the discounted cash flow is extended to the expiry of the lease. The average unexpired term of the Group's seven short leasehold properties is 14.0 years (31 March 2017: 15.0 years unexpired).

Sensitivities

As noted in 'Significant judgements and key estimates' on page 105, self storage valuations are complex, derived from data which is not widely publicly available and involve a degree of judgement. For these reasons we have classified the valuations of our property portfolio as Level 3 as defined by IFRS 13. Inputs to the valuations, some of which are 'unobservable' as defined by IFRS 13, include capitalisation yields, stable occupancy rates, and rental growth rates. The existence of an increase of more than one unobservable input would augment the impact on valuation. The impact on the valuation would be mitigated by the inter-relationship between unobservable inputs moving in opposite directions. For example, an increase in stable occupancy may be offset by an increase in yield, resulting in no net impact on the valuation. A sensitivity analysis showing the impact on valuations of changes in yields and stable occupancy is shown below.

	Impact of a change in capitalisation rates		Impact of a change in stabilised occupancy assumption	
	25 bps decrease	25 bps increase	1% increase	1% decrease
Reported group	£48.6m	(£44.9m)	£18.3m	(£19.1m)

A sensitivity analysis has not been provided for a change in the rental growth rate adopted as there is a relationship between this measure and the discount rate adopted. So, in theory, an increase in the rental growth rate would give rise to a corresponding increase in the discount rate and the resulting value impact would be limited.

Investment properties under construction

C&W have valued the stores in development adopting the same methodology as set out above but on the basis of the cash flow projection expected for the store at opening and after allowing for the outstanding costs to take each scheme from its current state to completion and full fit-out. C&W have allowed for holding costs and construction contingency, as appropriate. Four schemes do not yet have planning consent and C&W have reflected the planning risk in their valuation.

15. VALUATION OF INVESTMENT PROPERTY (continued)

Immature stores: value uncertainty

C&W have assessed the value of each property individually. However, two of the Group's stores are relatively immature and have low initial cash flows. C&W have endeavoured to reflect the nature of the cash flow profile for these properties in their valuation, and the higher associated risks relating to the as yet unproven future cash flows, by adjustment to the capitalisation rates and discount rates adopted. However, immature low cash flow stores of this nature are rarely, if ever, traded individually in the market, unless as part of a distressed sale or similar situation. Although, there is more evidence of immature low cash flow stores being traded as part of a group or portfolio transaction. Please note C&W's comments in relation to market uncertainty in the self storage sector due to the lack of comparable market transactions and information. The degree of uncertainty relating to the immature stores is greater than in relation to the balance of the properties due to there being even less market evidence that might be available for more mature properties and portfolios. C&W state that in practice, if an actual sale of the properties were to be contemplated then any immature low cash flow stores would normally be presented to the market for sale lotted or grouped with other more mature assets owned by the same entity, in order to alleviate the issue of negative or low short-term cash flow. This approach would enhance the marketability of the group of assets and assist in achieving the best price available in the market by diluting the cash flow risk.

C&W have not adjusted their opinion of Fair Value to reflect such a grouping of the immature assets with other properties in the portfolio and all stores have been valued individually. However, they highlight the matter to alert the Group to the manner in which the properties might be grouped or lotted in order to maximise their attractiveness to the market place. C&W consider this approach to be a valuation assumption but not a Special Assumption, the latter being an assumption that assumes facts that differ from the actual facts existing at the valuation date and which, if not adopted, could produce a material difference in value. As noted above, C&W have not assumed that the entire portfolio of properties owned by the entity would be sold as a single lot and the value for the whole portfolio in the context of a sale as a single lot may differ significantly from the aggregate of the individual values for each property in the portfolio, reflecting the lotting assumption described above.

Valuation assumption for purchaser's costs

The Group's investment property assets have been valued for the purposes of the financial statements after deducting notional purchaser's cost of circa 6.1% to 6.8% of gross value, as if they were sold directly as property assets. The valuation is an asset valuation which is entirely linked to the operating performance of the business. The assets would have to be sold with the benefit of operational contracts, employment contracts and customer contracts, which would be very difficult to achieve except in a corporate structure. This approach follows the logic of the valuation methodology in that the valuation is based on a capitalisation of the net operating income after allowing a deduction for operational cost and an allowance for central administration costs. Sale in a corporate structure would result in a reduction in the assumed Stamp Duty Land Tax but an increase in other transaction costs reflecting additional due diligence resulting in a reduced notional purchaser's cost of 2.75% of gross value. All the significant sized transactions that have been concluded in the UK in recent years were completed in a corporate structure. The Group therefore instructed C&W to carry out an additional valuation on the above basis, and this results in a higher property valuation at 31 March 2018 of £1,380.3 million (£77.0 million higher than the value recorded in the financial statements). The total valuations in the two Armadillo Partnerships performed by Jones Lang LaSalle are £3.3 million higher than the value recorded in the financial statements, of which the Group's share is £0.7 million. The sum of these is £77.7 million and translates to 48.8 pence per share. We have included this revised valuation in the adjusted diluted net asset calculation (see note 13).

16. TRADE AND OTHER RECEIVABLES

	31 March 2018 £000	31 March 2017 £000
Current		
Trade receivables	3,684	3,174
Capital Goods Scheme receivable	1,876	2,725
Other receivables	287	266
Prepayments and accrued income	12,739	11,877
	18,586	18,042
Non-current		
Capital Goods Scheme receivable	2,385	4,091

Trade receivables are net of a bad debt provision of £14,000 (2017: £7,000). The Directors consider that the carrying amount of trade and other receivables approximates their fair value.

The Financial Review contains commentary on the Capital Goods Scheme receivable.