Mineworkers’ Pension nears end of ‘difficult’ office sales

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25 mins ago

Investors

The UK pension fund is close to divesting all of its secondary office holdings as it looks to rebalance its overall real estate portfolio.

Evelyn Lee -

Mineworkers’ Pension Scheme is one sale away from liquidating all of its secondary office assets as it seeks to rebalance its overall real estate portfolio, *PERE* has learned.

Since Q4 2023, the UK pension plan, which owns approximately £1 billion ($1.28 billion; €1.17 billion) in real estate, has divested five secondary office properties totaling £94 million. These disposals include 25 Victoria Street in London, which was sold to BNP Paribas Real Estate Investment Management in December for £42.5 million; and Old Change House in London, which was sold to London-based Addington Capital and European private equity real estate firm BauMont Real Estate Capital for around £23 million in April.

Among the other assets are The Arc in Leatherhead, the BP North Sea headquarters building in Aberdeen, and Kingsmead Business Park in High Wycombe. A final secondary office sale is expected to be completed later this year.

Through the divestments, MPS has reduced its overall office sector exposure from 28 percent to 17 percent over the past two years. "There's been three main drivers behind the sales," said Dan Berger, director of property and funds at London-based manager Delancey, which was selected by Coal Pension Trustees to take over management of MPS's real estate portfolio from LaSalle Investment Management in 2022. Coal Pension Trustees is a company jointly owned by MPS and British Coal Staff Superannuation Scheme and acts as an executive for MPS.

One driver was the pension plan seeking liquidity and looking to reduce its allocation to real estate, after the UK's ill-fated mini-budget in 2022 led the country's defined benefit plans to become overexposed to illiquid assets, including real estate, and shift to high-yielding and liquid government bonds. Another was the negative outlook for some of MPS's real estate holdings. "We felt that the right thing to do was to sell if we could get the right price, because the forward-looking return for the client was going to be poor," he explained.

The third driver was a rebalancing of MPS's 41-asset property portfolio, which is "a very traditional, standard core portfolio" that Berger considered "overly diversified" on multiple fronts. For one thing, the pension plan had too many real estate assets, most of which were a smaller average asset size and lower quality. Additionally, the portfolio had sizable exposures to out-of-favor sectors like secondary office and secondary retail, given that core managers like LaSalle typically closely follow the benchmark index for sector allocations, he said.

The portfolio is also overly diversified geographically, Berger added. "While we've got the whole of the UK to play with as an investment universe, you don't need to be everywhere if the fundamentals or the outlook for those geographies are not as strong as others.

"These were the portfolio-level issues that we are starting to work through, and the sales are the start of underpinning that," Berger remarked.

Rebalancing plan

In rebalancing the portfolio, "the keyword is concentration," he said. Delancey aims to reduce the number of MPS's real estate holdings to approximately 20 and concentrate its sectors and markets.

From a sector perspective, the portfolio rebalancing has been most heavily focused on reducing the pension plan's exposure to secondary offices. Berger defines secondary office assets as those lacking the environmental credentials investors seek and the locations and configurations that occupiers require.

“They’ve been difficult to sell,” he said. “The investment market in general has been soft and certainly in these sectors, and for these assets, given challenges around the quality. We’ve been as aggressive as we can be in getting the best outcome for our clients and negotiating hard.”

In addition to liquidating the portfolio’s secondary office assets, the firm also aims to reduce the pension plan’s exposure to secondary shopping centers. “The yields are very, very high now in that sector, so there’s less pressure to sell because you are earning a reasonable level of income, but certainly over the longer term, that’s not a sector we’d be looking for strong exposure to,” Berger said.

Over the past two years, the portfolio’s allocation to industrial and logistics has increased from 30 to 37 percent, while its exposure to student housing has also grown from 7 to 10 percent. MPS’s allocation to retail warehouses has held steady at 20 percent, while the remainder of the portfolio is invested in long-lease, inflation-linked assets such healthcare facilities, hotels and social housing.

The firm plans to reallocate the portfolio to more attractive sectors such as logistics, which continues to have strong occupational demand and rental growth that will lead to higher overall returns. The firm also favors student accommodation, which has a supply-demand imbalance driving strong rental growth and defensive income. Another sector Delancey is bullish on is retail warehousing, which has strong occupier demand and is producing higher yields because of market repricing. “We think the total returns from those sectors are likely to outperform the broader real estate market, and certainly other sectors,” Berger explained.

In terms of the portfolio’s geographical composition, Delancey is pivoting away from secondary markets and focusing on London and other major UK cities. “From an investment perspective, that’s where the most liquidity is,” he said. Also, those markets generally have a greater diversity and depth of occupiers and can offer bigger and better-quality assets. “We’re on a journey of doing that, and we’ve got a fair way to go,” Berger said. “But that’s the direction of travel.”

Real estate accounted for 10.77 percent of MPS’s total assets under management of £10.58 billion as of September 30, 2023, according to the pension plan’s 2023 report and *PERE* data. Property represented the fourth-largest asset class for the pension plan, after public equities, private equity and fixed income, *PERE* data showed. MPS is among the 25 largest UK pension funds by assets under management, according to UK Parliament.