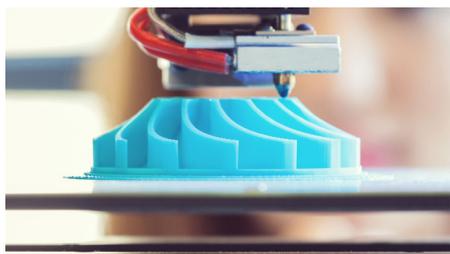


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Foreword

As we start to wind down and prepare for the festive period, the end of the year is a time to take stock and look ahead to the challenges and opportunities that lie ahead. Salamanca Group remains focused on exploring opportunities within the UK, predominantly in the real estate sector. This edition covers the impact of IFRS 16, an outlook on the UK property market and disruptive trends impacting the real estate arena. In addition, Lord Triesman, a fellow Director, and I were fortunate enough to spend time with the Cuban President on his visit last month and Lord Triesman's latest blog recounts his visit.

- **The IFRS 16 accounting standards** come into effect on 1st January 2019. All corporate companies who use rentals or leasing to access assets will be affected. *Are you ready?* Dena Bellamy, an expert in corporate finance, reviews the likely impact on P&L, key ratios and balance sheets.
- Despite Brexit representing a raft of challenges for the UK, London is seen as a world city and the UK a favourable market to conduct business. Simon Heilpern, Head of Real Estate, provides a brief overview of the **UK property market** which has a more positive stance than one may expect.
- Social trends and technological change are impacting the shape of the real estate industry globally. Traditionally a slow industry to adapt to change, Dominique Allnutt, Marketing Director, has identified a snapshot of these trends that are signposting the evolution of land development sites and business requirements. For sites in the UK, they need to move up a gear and **build for the future**.
- As the UK looks to establish new trading relationships around the world, we continue to explore opportunities in Cuba. Cuba is a market which is transforming and, whilst small, is a leading opportunity across central and south America. Lord Triesman delivers a **first-hand account of the Cuban Presidential visit** with appetite shown for establishing modern trading relations with the UK.

I wish you all a wonderful winter break and look forward to working with you in 2019.

Martin Bellamy
Chairman & CEO

Changes to lease accounting: A catalyst for change in corporate real estate strategy

By Dena Bellamy, Managing Director of Corporate Advisory

All corporate companies who use rentals or leasing as a way to access assets will be affected by IFRS 16 when it comes into effect on 1st January 2019. Those which lease high value assets in the retail, airline, transport and logistics industries are likely to be more greatly affected. Historically companies have made extensive use of off-balance sheet operating leases, which are often effected through sale and leaseback transactions, to optimise the balance sheet and maximise available cash for investment in the business and/or reducing debt. However, IFRS 16 will radically change the accounting treatment for these operating leases. *Are you ready?*

What is the impact?

IFRS 16 comes into effect for accounting periods ending after 1 January 2019, replacing IAS 17. The standard radically changes the accounting treatment for most operating leases. Henceforth they will be treated in a similar manner to finance leases, recognising right of use assets and associated lease liabilities on the lessee's balance sheet.

The accounting changes will apply to all companies who use rentals or leasing to have access to assets.

Those which currently lease high value assets such as real estate, manufacturing equipment, aircraft, trains and ships are expected to be most greatly affected.

The changes will have far-reaching implications for a company's financing and operations. The effects will be visible on both the balance sheet and on the P&L account, where the lessee will recognise the depreciation of the leased asset and interest cost instead of the operating lease expense.

	IAS 17		IFRS 16
	Finance leases	Operating leases	All leases
Revenue	££££	££££	£££
Operating Costs	---	Lease expense	---
EBITDA			↑↑
Depreciation & Amortisation	Depreciation	----	Depreciation
Operating Profit			↑
Finance Costs	Interest		Interest
Pre-tax Profit			↔↔

Likely Impact on Key Ratios		
↑ Gearing (Leverage)	↑ Debt/Equity	↑ Net Debt/EBITDA
↓ Current Ratio	↓ ROCE	↓ Asset Turnover

	IAS 17		IFRS 16
	Finance leases	Operating leases	All leases
Assets	🚚 🖨️	---	🚚 🖨️ 🏢 🏭
Liabilities	££	---	££££
Off Balance Sheet	---	🚚 🏭	---

The accounting changes will impact most financial ratios and potentially affect debt covenants and credit ratings, and public perceptions.

How to action?

Companies are well-advised to undertake a fundamental re-evaluation of their corporate leasing strategy. For example, the benefits of sale and leaseback transactions will be diminished with the adoption of IFRS 16 as virtually all off-balance sheet accounting for lessees will be eliminated.

With appropriate financing, asset ownership can be a more cost-effective solution. This also offers greater control and flexibility over the use of the asset.

Through our Corporate Finance and Real Estate experts, Salamanca Group is able to offer strategic advice and assist with the arrangement of innovative financing solutions for companies who are currently lessees of property or plant. Our support enables companies to (re)purchase their commercial real estate, as well as businesses which already own commercial real estate and are looking to release cash from these assets.

A snapshot of the UK property market

By Simon Heilpern, Head of Real Estate

Brexit continues to be the focus of headlines and most conversations, and rightly so. The vote is imminent, and the outcomes continue to become less certain both in terms of nature and extreme. However, it is important to highlight the underlying pace of economic growth remains resilient and the UK property market is performing well. Salamanca Group retains a positive stance towards the health of the property market almost regardless of the outcome of Brexit for the reasons twofold:

- London remains one of the top financial cities in the world
- The UK remains a robust and stable market known for its favoured time zone, legal system, trusted financial regulator and ease of doing business

Clear evidence of the market's positive health is shown through investment pricing, volumes to date and market performance.

- Over the first ten months of 2018 the City of London **investment market volume of transactions reached its highest level ever** for that period (£9.47bn, 7.6% up on the same period in 2017)
- Across all commercial property sectors London retains its crown as the world's most popular destination for cross-border investment into real-estate, with **inward volumes more than 50% higher than Manhattan, US**
- The occupational market remains strong with 8.9m sq ft leased in the first nine months of 2018. This is only 4% down on the same period in 2017, which was the strongest ever year in the central London occupational market*
- The only surprise lies in the lack of upward rental growth which would be expected given the low vacancy rates and restrained development pipeline

Despite these healthy statistics, Brexit is powerful enough to cause pause for thought and in the worst case a change in activity and sentiment. So, whilst there is no cause for complacency, we see a strong UK and London in particular, and its place in the world order will remain powerful.

As the future unfolds, Salamanca Group is excited by the measured openings that should emerge in the UK. Salamanca Group is involved across a mix of real estate assets – light industrial, offices, retail, hotels and residential. Whilst specific characteristics effect each sector, we are confident that capital will be quick to take up opportunity particularly in a low sterling exchange environment.

Salamanca Group holds a prime real estate advisory capability merged with in-depth property expertise across use class and location. Unusually for the property market this is combined with significant corporate advisory experience. This corporate and property combination yields the potential to identify added value and develop corporate strategic to drive and to capitalise on any opportunistic returns that emerge.



Salamanca Group sits at the epicentre of real estate markets offering both expert corporate understanding and real estate transaction experience.

**All statistics sourced from Savills 2018*

Building for the future

By Dominique Allnutt, Director of Brand, Marketing & Communications

Whether a business, logistics or manufacturing park, the shape of the commercial industry from light industrial through to advanced manufacturing, warehousing and office space is on the cusp of change driven by buyer and employee demand, new regulations and automation. We're increasingly immersed in an information centric world and whilst industry 4.0 focuses on the use of smart technologies which is impacting both building and land plot requirements, social change is also contributing to the future of commercial buildings and the environments in which they are located. As recent owners of a 635-acre mixed-use commercial site in the UK, we've identified a snapshot of social trends, transformative technology and considerations that are signposting the evolution of both the traditional commercial park and business requirements.

Social trends:



E-commerce

E-commerce is growing by 10% each year. In the UK, van traffic has grown by 71% over the

last 20 years, compared to a 13% growth in cars. Considerations for transport solutions and sustainable growth are important factors for considering warehousing space, location and functionality.



Placemaking

There is demand for increasingly attractive places of work to boost employee well-being. Developing healthier and happier places to work includes

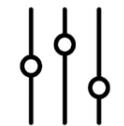
space for breaks, changing facilities, cycle storage, more natural light indoors, availability of outside space, improvements in landscaping and air quality – a 180° spin on the sterile, car dominated monoculture.



Clean Growth

Sustainable economic growth is at the heart of the UK's industrial strategy and supported

by investors and the population – 85% of people in the UK would like to make changes to be green. The Clean Growth economy is forecast to grow four times faster than the projected growth of the UK economy with a focus on cleaner and smarter ways of providing power, reducing transport emissions and improvements to heating and cooling of buildings.



Personalisation

Demand for personalised and customized goods is increasing. Items which

are usually produced on mass, may now have two or three production processes, which may not be delivered in the same manufacturing space. This is forcing a merge of relationships from the human to the machine – the evolution of industry 5.0.

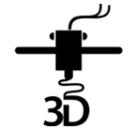
Technology transformations:



Artificial Intelligence

A new age of digitally enabled manufacturing where artificial intelligence

and augmented reality improve manufacturing processes. New products and processes can be virtually tested, errors and downtime reduced, waste reduced and safety improved. It also helps lower skilled workers perform traditionally higher skilled roles by teaching on the go.



Additive manufacturing/3D printing

3D printing enables the manufacturing of parts

without the need for moulds and is increasingly becoming a mainstream mass production method being used to reduce costs, increase speed of delivery, make logistics more efficient and environmental improvements.



Big Data

Digitisation and a drive to use big data is a growing trend to tackle logistical inefficiencies

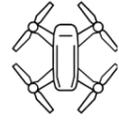
and modernise the supply chain. With 15-20% of trucks on the road empty and time wastage during offloading and unloading, an end to end visible supply chain is an opportunity to reduce empty miles. In addition, supply chains can also use big-data to have a more holistic understanding of stock items allowing for faster response to demand spikes.



Robots and cobots (collaborative robots)

Robots are transforming logistics and e-commerce companies

to carry out low-value tasks in warehouses 24/7, allowing human workforce to focus on value-add activities. What has taking a while to get off the ground, has now picked up pace. This year alone Google invested \$500m into automated logistics for JD, and Alibaba invested \$15bn into its own logistics infrastructure.



Drones

Drone technologies (aerial robots) are now being taken seriously by those in the logistics

and last-mile deliveries field. It is common knowledge that Apple, Microsoft, Intel, Amazon, DHL, Google and Uber are trialling and developing aerial delivery networks to speed up delivery times for groceries and food stuff. Amazon announced in October an expansion of its UK R&D with 1000 new roles to work on Prime Air. Air regulations are still a barrier to entry, so we may still not be seeing drone delivery take-off soon but middle to long term.

Future considerations:

Strategically located flexible space

Proximity to customer base, delivery efficiencies, keeping up with demand and increasing supply chain efficiencies are all evolving factors contributing to a dynamic requirement for space. Sites and tenants will need to respond to this flexible requirement as well as the blurring of boundaries between uses; the merge of office, R&D, and light manufacturing space as industry 4.0 evolves into 5.0 seeing more collaboration of humans and robots; and, the merge of factory and retail as factory outlets grow in popularity.

Mixed-use places

To attract and retain talented workforce, mixed-use places with amenities, a well-landscaped public realm and leisure facilities are becoming a prerequisite. These are designed to bring people together to offer synergies for collaborations, shared workspace and a healthier lifestyle.

24/7 access

The on-demand nature of the internet and the ability for robots to be working during traditionally unsocial working hours, results in building usage all hours of the day requiring solutions for energy and noise management, security, and out of hours transport solutions.

Provision of dark fibre and data centres

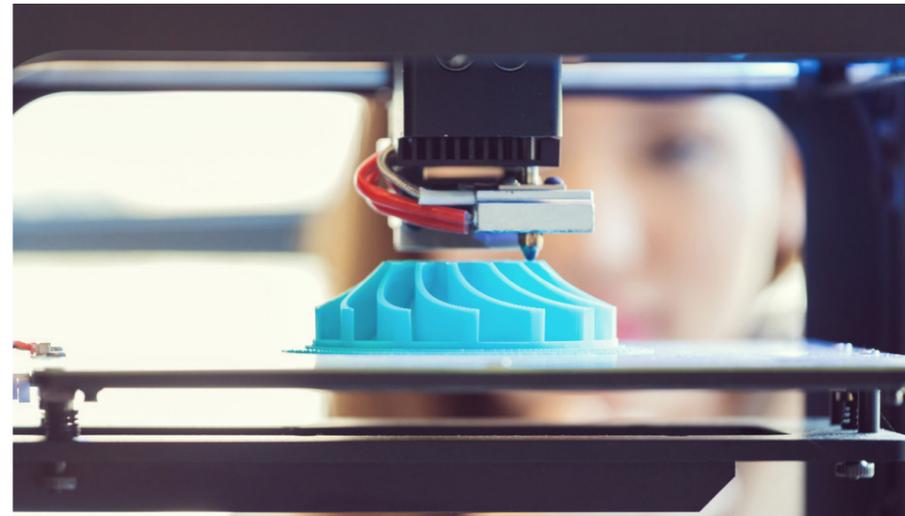
The importance of access to data is critical and future-proofing for data growth to ensure performance, security and super-fast access is a large consideration. The advantages of dark fibre have led to an increasing demand from medium and large businesses.

Resilient energy solutions

Businesses are requiring more energy and access to resilient and cheap power to sustain business delivery, enable new technologies and data applications. Meanwhile carbon efficiency methods are becoming more widespread through retrofit and new building designs to improve heat and thermal storage and, embedding sustainability into asset management via smart energy management systems and using sustainable products such as energy efficient LED lighting.

Integrated and intermodal green transport solutions

In line with Government objectives, the UK should anticipate for a transformational shift to cleaner transport methods for both employee travel to work (on foot, by bike, electric car, shuttle bus, train) and logistics (hydrogen fuelled HGVs, train, e-bike, drones). Driverless cars may also require increased space for drop-offs. This multi-modal transport offer will define the future.



For references to data sources please contact, info@salamanca-group.com.

A first-hand account of the recent Cuban President's visit to the UK

By Lord David Triesman, Group Director

It would be hard to overstate the importance of the visit of President Miguel Diaz-Canel to the United Kingdom in mid-November. A trip originally scheduled as a stopover forming part of a more extensive global journey, developed into a significant visit not least because Diaz-Canel is new Cuban President, but he was also the first ever Cuban President to visit the UK.

The Far Eastern leg of the delegation which included Vice President Ricardo Cabrisas among other senior Ministers focused on trade, diplomatic and sporting relations. The visit took in China and President Xi Jinping, Russia and President Putin, Laos and President Bounnhang Vorachith and Vietnam and President Nguyen P'hu Trong. Understandably, we focus this account on the visit to the UK and the development of the relationships which can be achieved here and in Cuba and that route of travel is now mainstream.

“He started the morning with a visit to the Abbey Road Recording Studios, a small homage to the Beatles including the obligatory photo on the zebra crossing.”

Diaz-Canel had meetings with the Chancellor, Philip Hammond, Trade Secretary Liam Fox and Prince Charles. Earlier this year, Philip Hammond took a significant step as Foreign Secretary as the first top leadership Minister to visit Cuba in over half a century. The other dates with UK Ministers were directed at normalising trade, cultural and sporting relationships. I was fortunate to spend almost the whole time with the President on his main day of the visit.

He started the morning with a visit to the Abbey Road Recording Studios, a small homage to the Beatles including the obligatory photo on the zebra crossing.

From there to a full meeting of the Cuba Initiative – an independent, bi-lateral body that supports trade and investment between UK and Cuba - which I have the honour of chairing for a detailed discussion of his priorities for the economic growth of his country. The business audience of course had their advice and perspective and it was a positive discussion. I had agreed in advance with Vice President Cabrisas on the need for a relaunch of the Cuba Initiative in the first half of next year, a proposal enthusiastically endorsed by Diaz-Canel.

I was particularly pleased to hear his explicit support for the formation of the new investment bank, a joint venture between Salamanca Group and Havin Bank, in Havana and which will steer many of the major projects central to economic growth. Everyone was conscious that however much interest there is in Cuban business development, it will take careful advisory and structuring work to succeed and the Cubans have decided that a shared joint venture with London know-how is the place to start.

From the Cuba Initiative, we went to the first of several meetings in Parliament involving about 200 parliamentarians from all parties as there is no ideological difference about the value of the approach to both countries. There was once again sharp interest in the plans

Cuba are making and the joint venture designed to help make them a reality. President Diaz-Canel set out the proposal once more to this large political audience and it was good to see the level of agreement among them. In subsequent days parliamentary colleagues have told me they see a new mood and much improved mood music.

“Cuban business development will take careful advisory and structuring work to succeed and the Cubans have decided that a shared joint venture with London know-how is the place to start.”

Our second meeting was a discussion with three of the sectors the President is eager to engage in part because of his personal interest. The University sector was represented by Baroness Val Amos and two colleagues providing strong insights to the joint projects on which we all could build. Sir Hugh Robertson, a former Sports Minister and current Chairman of the British Olympic Committee expressed both his welcome for deeper sporting relationships and delivered a message from Seb Coe



that he would meet the Cuban Olympic Committee in Havana in the spring. Baroness Deborah Bull, now a pro-Vice Chancellor at Kings College London and a former Prima Ballerina who has worked with some of the most eminent Cuban dancers, set out a vision of further shared projects and art education. All were warmly received by the Cuban delegation and we agreed that the themes of education, sport and the arts should play a far greater role in the future of the Cuba Initiative.

Diaz-Canel then had a meeting with Jeremy Corbyn before a round of evening engagements.

“Themes of education, sport and the arts should play a far greater role in the future of the Cuba Initiative.”

Of course, meetings are simply the prelude to doing the real things. It is clear Cuba needs to develop in several areas where it has skills and resources. The meetings discussed green energy, climate protection, tourism, food security, the growing successes in pharmacology especially in cancer treatments and diabetes. We covered the changes in Cuban commercial law and taking the burden out of start-ups and regulation. As might be imagined there was a good deal of discussion of the new investment bank now nearing its first operational input.

If the UK does leave the EU, if the discussions on the Customs Union prove fruitless, if we stumble into a no deal conclusion with all its consequences, the issue of new trading opportunities will become ever more pressing. The paradox is surely that the good sense of generating better trading is in any case desirable. Cuba is a market which is transforming and whilst small is a leading opportunity across central and

south America. So, the effort makes complete sense and this Presidential visit demonstrates Cuban appetite for modern trading relations. The USA doesn't seem to appreciate this; but we do.

Lord David Triesman has over 40 years' experience working with Cuban leaders and their ambassadors in London, strengthened relationships when responsible for Anglo-Cuban relations as a Foreign Office Minister in the mid-2000s and deepened these with time. The development of such a trusted relationship with partners in-country, aided by a long term vision and presence, has allowed Salamanca Group to be part of the opening of Cuba to foreign investment.

Lord David Triesman is leading this initiative and has developed a blog to provide an assessment of progress and opportunity as we create, together with the Cubans, a new financial hub. Previous blogs are available on the Salamanca Group website.

Strategic Insight Events

This year we continued to host the Strategic Insight breakfast series with the European Leadership Network (ELN). The meetings bring together a small number of business leaders, leading political figures and senior ambassadors to discuss key issues facing Europe's security climate. Our latest event focused on:

Digitisation of Security

Chaired by Des Brown, former Defence Minister, with two guest speakers. John Vine, a former Chief Constable of Tayside and Chief Inspector of Borders and Immigration at the Home Office. He spoke alongside Alistair Treharne, who is currently an Identity Advisor to the World Bank and the UK Government.

The speakers guided guests through the risks and barriers faced by governments and the private sector with digitalising our security.

The next Strategic Insight breakfast will be held in the new year. If you are interested in attending, please contact info@salamanca-group.com

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We welcome the opportunity to discuss any questions you may have in regards to the articles in this newsletter, and to discuss your business and/or personal requirements.

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