Results analysis: Picton Property Income

PCTN delivers capital and income growth...

Update
23 May 2025

- **Picton Property Income (PCTN) has released its results for the year ending 31/03/2025, recording a NAV total return of 8.1% and profits of £37m. PCTN's property total return was 7.3% for the year, compared to 6.3% for the MSCI UK Quarterly Property Index. This marks the 12th consecutive year PCTN has outperformed the property index. Net assets were c. £533m at the year end.**

- **The NAV per share increased 4.2% to 100p (2024: 96p) and dividends for the year totalled 3.7p (2024: 3.5p), a 5.7% increase. Dividends were covered 113% (2024: 114%). This results in an NAV total return of 8.1%. PCTN's share price total return was c. 16%, with the discount narrowing from c. 32% to 28%. The dividend yield at the current share price is c. 5.1%.**

- **PCTN received £51m of gross proceeds from disposals during the year, comprising of three repositioned office assets. The average disposal price was at a 5% premium to the March 2024 valuation.**

- **PCTN's gearing reduced to 24% LTV (2024: 28%) with the short-term revolving credit facility (RCF) fully repaid using some of the proceeds from disposals. As a result, the weighted average interest rate fell to 3.7% (2024: 3.9%) with all debt maturing in 2030/2031. Currently the RCF is undrawn but was refinanced during the year and gives a further £50m of debt to draw upon.**

- **In January 2025 PCTN initiated a share buyback programme, and to date has repurchased £11.7m worth of shares. PCTN issued a sperate statement at the same time as the final results noting that the programme has been extended to a maximum of £17.5m to run until the AGM in July 2025, when the authority to buy back further shares will be renewed. Buybacks have been executed at significant discounts to NAV and are earnings and NAV enhancing.**

- **PCTN's reversionary rental potential is 16% higher than contracted rental, or £7.5m. Of this, £4.1m is where contracted rents are below estimated rental value (ERV) and £3.4m is from space available to rent.**

- **Following disposals, PCTN's exposure to offices has fallen to 24% (2024: 28%) and almost two thirds of the portfolio is invested in industrial, warehouse and logistics assets. These sectors are the source of much of PCTN's reversionary potential noted above and continue to see strong tenant demand balanced by limited supply of new stock.**

- **Michael Morris, chief executive said: "We have made further progress repositioning the portfolio, improved occupancy to 94% and reduced office exposure by a fifth, with £51 million of disposals ahead of March 2024 values. Alongside share buybacks, we have used these proceeds to repay debt, reduce financing costs and invest to improve our assets. Looking forwards we will seek to grow earnings through further disposals of low yielding assets and accretive redeployment of capital. Our significant reversionary potential in the portfolio, combined with our long-term fixed rate borrowings, puts us in a strong position to deliver income and value growth."**

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Kepler View

As the discount chart below illustrates, UK commercial real estate as an asset class has suffered from negative investor sentiment since the start of the period of higher interest rates, and **Picton Property Income (PCTN)** is far from being alone in trading at a significant discount to net asset value. The pace of M&A activity in the REIT sector over the last few years has been fierce, with the supply of diversified UK REITs such as PCTN having shrunk as buyers with a longer-term perspective have taken advantage of what they see as the stock market's excessive pessimism, with a series of take-privates and mergers.

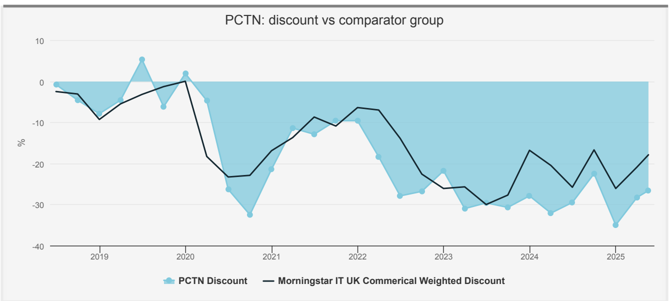
While it's hard to fight against macro headwinds, PCTN provides a case study of how active asset management can create value, with the disposal programme referenced above made more successful by PCTN's strategy of walking assets through the process to allow a change of use, with office assets in good city locations being granted change of use permission to be repurposed for residential or student accommodation. This is a sufficiently time consuming and complex process that getting assets to this point adds enough value to justify disposal above carrying value, meaning PCTN captures some of the upside value without having to go though an extensive capex programme on vacant assets. This is important for PCTN as one of its primary goals is to maintain and grow a fully covered dividend, and this year it has grown the dividend by almost 6% while keeping cover at 1.13x.

This process has continued into the current financial year, with PCTN announcing in May that it has secured approvals through permitted development rights to add a floor of residential accommodation above one of its largest assets, a London office in EC1. While it remains to be seen whether PCTN follows the same strategy and uses this as a lever to dispose of the asset remains to be seen, but whether it chooses to redevelop itself or take the premium in a disposal, the outcome will almost certainly be accretive for shareholders.

Meanwhile, those macro headwinds that have led to the discounts referred to above are abating and PCTN reported a rise in property values this year, on top of further rental growth, which has continued every year through this period of discounts. Further, PCTN has reduced the size and cost of gearing and has sufficient firepower to continue to buy shares back. By our calculation the shares are currently at a 28% discount, which means buybacks will be highly accretive to NAV and earnings. Moreover, the UK has cut interest rates once again recently, which could be the start of a period of discounts on REITs narrowing further. Weighing up all the factors, including increasing values, rental growth, active disposals, increasing dividend, PCTN's discount looks to us to be unduly pessimistic at this point in the cycle.

Note that the chart below shows PCTN's discount compared to the AIC's UK commercial property sector. PCTN is not part of this peer group but it provides relevant context to PCTN's discount.

Fig.1: Discount



Source: Picton, Kepler Partners, Morningstar

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