

Title of meeting: Cabinet
City Council

Date of meeting: 1 October 2024 (Cabinet)
15 October 2024 (Full Council)

Subject: Portico Shipping Ltd Review

Report by: Mike Sellers, Port Director

Cabinet Member: Councillor Steve Pitt, Leader

Wards affected: All

Key decision: Yes

Full Council decision: Yes

1. Purpose of report

- 1.1 As required by Full Council, Cabinet is required to undertake a periodic strategic review of the options for the use of the Portico site and therefore the continued operations of Portico Shipping Ltd (Portico).
- 1.2 Accordingly, this report provides a full options appraisal and financial evaluation (including risks) prepared over a 20-year period of all of the available options for the use of the Portico site. The evaluation has been informed by an independent strategic review undertaken by an established expert consultancy and that review has been subject to scrutiny by the Company Advisory Board.

2. Recommendations

2.1 Full Council recommendations:

- 2.1.1 The Council approves Portico's investment requirement of £20m over the next 10 years, to deliver an overall return at today's value (net present value) of £4.4m during the period 2024/25 to 2033/34, and agrees to finance this, as follows (subject to recommendations 2.2.2, 2.2.3, 2.2.4 and 2.2.5 below):
- £1.9m funded from Portico's existing loan facility;
 - £13.6m funded from an increase in Portico's loan facility; and
 - £4.5m funded directly through the direct acquisition by the Council of equipment and lease to Portico on commercial terms.

2.1.2 That the Council's Authorised Limit (the maximum amount of borrowing permitted by the Council) and the Operational Boundary (the maximum amount of borrowing that is expected) approved by Full Council on 13 February 2024 is increased to accommodate the phasing of Portico's £20m investment requirement.

2.2 Cabinet recommendations:

2.2.1 The Council retain Portico and that the amended budget (Section 6, Option 1) is adopted as the Council's preferred option.

2.2.2 Updated subsidy control advice is gained by the Council.

2.2.3 The Council loan is provided on terms and at a rate consistent with subsidy control legislation.

2.2.4 Any draw down on the loan facility by Portico is subject to the following:

- i) A rolling annual review of the 20 Year Business Plan demonstrating the continuing viability of Portico and that the continued operation of Portico continues to deliver the best financial return compared with all other viable alternatives
- ii) The Capital Investment is necessary either for the sustainability of existing income streams or for the generation of additional income.
- iii) Any proposed Capital Investment itself represents the most favourable return when assessed against the balance of:
 - The financial return on a Net Present Value basis and over the whole life of the asset created versus other potential options for the same outcome.
 - The relative risk of each alternative option.

iv) Approval by the S151 Officer.

2.2.5 Continued parent company support and the availability of the loan facility is subject to the annual review by the Company Advisory Board, and approval of a satisfactory Budget and 3 Year Business Plan, which must demonstrate to the shareholders satisfaction that:

- The assumptions that underpin the 3 Year Business Plan are robust with a more than reasonable chance of being achievable.
- That the 3 Year Business Plan is prepared to illustrate the financial effect of reasonable optimistic and reasonable pessimistic scenarios, in order that the shareholder is aware of the reasonable range of risk associated with the "Base Case" Business Plan.

- Recognising the exposure of the company to cyclical trade factors and adverse weather, that the overall 3 to 5 Year financial results of the Company provide an overall net return to the Shareholder over the period taking into account all returns received by the Shareholder through rents, dues and all other income elements of services provided by the Shareholder (including the Portsmouth International Port (PIP)).

2.2.6 The Council keeps under review the returns that would reasonably be expected to be achieved from alternative uses of the site, undertaking a formal review at the earlier of every 5 years or an expectation that the financial performance set out in recommendation 2.1.1 above is unlikely to be achieved.

2.2.7 Portico is restructured, to include the creation of subsidiary companies and a holding company, as recommended by the independent review, to enable the business to remain competitive, and meet market needs.

2.2.8 It is noted that the Portico operation provides additional volumes for pilotage and towage which supports the need for a dedicated service for both aiding PIP cruise and ferry.

3. Reasons for recommendations

3.1 It is recommended that continued operations and investment into Portico is approved for the following reasons:

- i) All viable alternative uses for the site have been evaluated
- ii) The annual return to the Council as a whole is forecast to become positive from 2027/28 and Portico is forecast to become profitable in its own right in 2031/32.
- iii) Over the next 10 year investment period the Portico Business Plan is forecast to generate an overall return of £4.4m at today's value
- iv) Retaining Portico, based on its Business Plan, is forecast to provide an overall financial return to the Council 7 times greater than the next best alternative when modelled over 20 years after taking account of all necessary financial support and investment
- v) The Portico Business Plan has been based on prudent assumptions
- vi) It is expected that the overall risk attached to continued operations of Portico and delivery of its Business Plan is similar to all other alternatives

4. Background and Context

- 4.1 Portico, previously called MMD Shipping Ltd, was acquired by the Council in 2008. The company is located at PIP and operates from the deep-water cargo shipping channels.
- 4.2 The Council's rationale for acquiring MMD was threefold; namely:
- To maintain the income streams to the commercial port;
 - The evaluation (endorsed by external advisors) that the company could be turned around and have good financial prospects; and
 - The investment was considered a strategic land acquisition to future proof the commercial port for future development, adjacent to deep water quays.
- 4.3 The Council is required to keep under review the returns that would reasonably be expected to be achieved from different uses of the site from where Portico operates. In 2018 the Council carried out a review of alternative uses of the site, to identify whether or not there was a realistic prospect that a better financial return could be obtained at lower risk from alternative uses. As part of that review the Council commissioned an independent expert to review Portico's Business Plan to provide confidence that the evaluation was robustly based. The review determined that the best return for PCC was to support Portico's Business Plan which included a strategy of diversification of cargoes to handle in order to both respond to market demands and improve revenues but also to reduce the level of risk associated with reliance on a small number of cargo types.
- 4.4 Following the review and in accordance with its recommendations, in February 2019 PCC Cabinet and Full Council approved Portico's Business Plan which included an agreed a loan facility of £15m to deliver a return of £19.3m over the 5-year period. This financial support was subject to a number of financial governance conditions including the requirement to provide a three-year business plan to the Council for approval together with a 20-year forecast, satisfactory capital investment appraisals and compliance with state aid rules.
- 4.5 Financial performance against the business plan has been lower than anticipated and so last year the Council approved the company's Business Plan for 2023/24 and continued financial support but conditional on the prospects for the company under the Business Plan remaining positive, and a further strategic review of the company's Business Plan against viable alternatives, to ensure best value.
- 4.6 Despite successfully progressing its diversification strategy, Portico continues to require financial support from the Council by way of an annual revenue contribution which in 2023/24 amounted to £5m. In addition, the Council also provides a loan facility (within the sums approved by Full Council and subject to conditions) to allow Portico to invest in capital infrastructure. This is necessary so that Portico can continue to adapt to a changing shipping market, which is becoming increasingly containerised on larger vessels as well as diversifying its customer base.

- 4.7 The financial performance against the business plan has been lower than anticipated due to a number of factors including a global recessionary impact on trade, a reduction in land availability (to drive revenues) due to the port's construction of a Border Control Post, delays to border changes under Government policy and planning delays for the development of Aggregates Terminal. Overall, this had a negative impact on income to Portico over the past 5 years, estimated at over £12m. This was mitigated by a number of measures including active marketing, expansion of the company's commercial team, and the identification of a wide range of staffing and other operating expenditure savings.
- 4.8 Portico still continues its pursuit of diversified cargo handling (as previously recommended), utilising its skilled workforce and heavy lift capabilities. Its cargo portfolio now includes containerisation, aggregates, agribulks, project cargoes and ad hoc general cargo, in addition to fresh produce. The company remains the market leader for the UK's bananas. Portico has also looked to diversify its business operation to include Portico Logistics. This branch of the organisation incorporates logistics services, such as customs agency, freight forwarding, transport, and warehousing. These diversifications have significantly de-risked Portico's business model as well as providing greater opportunity of sustainability of the business into the future.
- 4.9 In accordance with Full Council's requirements, the Council commissioned Fisher Associates to undertake a strategic review of all of the available options for the use of the Portico site, including the continued operations of Portico Shipping Ltd (i.e. its operational and financial performance, Business Plan and governance) and any synergies that may exist between Portico and the Port.

5. Summary of Fisher report

- 5.1 The Fisher report identified a number of strengths and opportunities that could be exploited by Portico, working more closely with PIP and involving some re-organisation that could inform the overall options appraisal of alternatives (see Section 6)
- 5.2 The current delivery model is essentially a private limited company port operator (Portico), working within a municipal harbour authority and alongside an adjacent port operator (PIP). Fisher does not recommend that this continues.
- 5.3 Portico has a strong and experienced team of managers. The control of costs is well managed; however a significant amount of management time is spent on dealing with processes to separate transactions between Portico and PIP, which suppress productivity.
- 5.4 The review and discussions around operations provides clear evidence that there are many efficiencies to be had by PCC through closer coordination between PIP and Portico. This could free up resources and support higher productivity and business growth.

- 5.5 The report recommended that Portico is restructured with the landlord harbour administration (PIP) and a Port Services Provider (Portico Port Services), and a logistics company (Portico Logistics).
- 5.6 Taking into account all other options (the options appraisal (Section 6)), there are substantial additional potential benefits arising from: a) Exploiting potential synergies and b) Further investment in the Portico estate.

6. Options Appraisal

- 6.1 The evaluation that follows builds on the work undertaken by Fisher Associates. The Council has carried out a review of Portico, and the alternative uses of the site, where Portico operate, to identify how the council can gain the best financial return, and whether or not there is a realistic prospect that a better financial return could be obtained at lower risk from alternative uses.
- 6.2 The long list of options identified, included 'do nothing', retain Portico and implement synergies between PIP and Portico, cease operating Portico and leasing land for industrial use and cease operating Portico and building houses on the Portico site.
- 6.3 The 'do nothing option' was dismissed as the option wasn't sustainable. The housing option was also dismissed due to the area being outside of the local plan, and the economic importance to the City and the region of maintaining the deep water berths.
- 6.4 The short list of options identified are summarised below:
- **Option 1: Retain Portico.** This option is based on Portico's business plan and includes many of Fisher Associates recommendations including implementing synergies between the Port and Portico and adjusted for local knowledge and prudence. This includes ongoing capital investment into Portico of £20m over the next 10 years.
 - **Option 2: Put Portico into liquidation. Rent site for industrial use.** This option would involve putting Portico into liquidation and Portico's customs agency staff transferring to PCC. Some of the assets used by Portico would be sold, and the site would be rented out. This option would require an element of capital investment and negotiation of rent with suitable tenants.
 - **Option 3: Do Minimal (Put Portico into liquidation).** This option involves putting Portico into liquidation and Portico customs agency staff transferring to PCC. Portico assets would be sold, and no operations would take place on the Portico site.
- 6.5 A summary of the financial appraisal is set out in Exempt Appendix A. Each option has been modelled on a Net Present Value (NPV) basis over 20 years. NPV is a

recognised method of comparing options which have differing cost profiles and differing income streams over a specified period of time. The method provides a comparison of costs and income (both capital and revenue) on a like for like basis by bringing the total financial effect of each option back to a single comparative value. The appraisal also seeks to evaluate the relative risk of each option to enable a balanced judgement to be made on both risk and reward.

- 6.6 The options appraisal has identified that in both financial and risk terms, the best option by a considerable margin, is to retain Portico. The defining financial consideration for the Council is the total return to the Shareholder (often referred to as the "net benefit"). This takes into account all other income streams to the Council derived as a direct consequence of operating Portico, net of all costs in deriving that income and is described below:

Portico Profit / Loss

- + Net Income to Port (from port dues etc.)
- + Net Income to PCC (from rent and interest on loans and leases etc.)
- +/- Dividend / Financial Support
- PCC Capital Financing Costs

= Total Return to Shareholder (Portsmouth City Council)

Accordingly, Portico's profit / loss is not the same as the return to PCC, rather it is one component of the overall return to which other income streams and costs are added. It follows therefore that a Portico loss does not necessarily translate into a negative return for PCC.

- 6.7 The overall return to the Shareholder of retaining Portico (Option 1) over the next 20 years is forecast to be £30.1m at today's value, being 7 times greater than the next best alternative option modelled.
- 6.8 A sensitivity analysis has been undertaken on Option 1 to understand a range of possible alternative financial scenarios in relation to the retain Portico option. Even under low case scenarios related to Option 1, the best option in financial terms is still to retain Portico.
- 6.9 Within the overall financial evaluation of continuing to operate Portico (and included within the NPV evaluation), is the requirement for an overall £20m of capital investment over the next 10 years, and £38m (cumulative) over 20 years. This will enable the company to become more efficient, meet the needs of customers moving to containerisation, and allow Portico to continue to diversify its business. This report

recommends the Council continues to invest in Portico, but subject to strict criteria as outlined in Section 2 of this report. The necessary capital investment required in order to drive the anticipated income streams includes:

- Investment in plant and equipment.
- IT hardware and software.
- Re-designing and improving the terminal to make operations more efficient and effective; and
- Investment to enable Portico to continue to diversify its operations into general cargo.

The business plan also identifies the need to invest in new cranes at Portico, which would be leased from PCC on commercial terms.

- 6.10 The investment in Portico will have a residual value and would be of use for some of the alternative options. This means that should Portico not realise its business plan, and in future an alternative option became financially better for the Council to pursue, a proportion of the recommended investment in Portico would remain of value to the Council.
- 6.11 The options appraisal has included assessment of restructuring Portico, which Fisher Associates recommends. This will allow Portico to remain competitive, meet market needs, and maximise the return to the Council. This restructuring would see the creation of subsidiary companies and a holding company, to include a company focused on shipping, a company focused on freight logistics, and a company focused on providing a range of complementary services. It is not the intention of the restructuring to give rise to redundancies, and nor to be of detriment to skilled posts at Portico. Please see Exempt Appendix B for further information.
- 6.12 Other aspects of the overall evaluation including the strategic fit, financial evaluation, key risks and opportunities of the recommended option to retain Portico, is summarised in the below table:

Strategic Fit	Financial Evaluation	Risk	Opportunity
The site where Portico operates continues to be used as a deep water facility, which is an important requirement of the planning authority.	Portico's 20-year plan sees the company move into profit. The recommended option translates to a NPV to PCC of 7 times greater than the next best	The overall risk of the Portico operation has been assessed as medium. Portico's strategy will provide a better spread of cargo mix at Portico, which will de-risk the reliance on palletised fruit.	Attract additional container / feeder services. Attract general cargo in addition to more fresh produce. Complete redesigning the terminal to make

<p>Portico’s planned investment meets the needs of the fresh produce market, by providing facilities to meet the needs of customers moving to containerisation.</p> <p>Planned investment also meets market demand for more capacity on the south coast for general cargo.</p>	<p>alternative use of the Portico site.</p>	<p>The largest risk is Portico isn’t able to retain and attract custom. However, the profitability of Portico would need to reduce by a considerable amount before retaining Portico was not financially the best option.</p> <p>Capital investment at Portico has been assessed as low risk because of the non-specialised nature of much of the investment, and some of the investment, such as equipment, could be sold.</p>	<p>operations more efficient and effective.</p> <p>Expansion through activities outside of Portsmouth.</p> <p>Restructure to allow Portico to remain competitive, meet market needs, and maximise return to the Council.</p>
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7. Governance

7.1 Portico has recently undertaken a review of its corporate governance, Board structure and Articles of Association. This was set out in a report to Cabinet on 14 February 2022. Portico’s Board now includes independent Non-Executive Directors, to provide independent external expert input to the company and hold the Executives to account.

7.2 The current structure of the Portico Board and appointments is as follows:

- **Camilla Carlbom Flinn – Chair, Independent Non-Executive Director**
Camilla is a Director of Pentagon Maine Ltd, a supply chain logistic provider. Camilla is also Honorary Consul for Sweden for Humberside, Lincolnshire and Nottinghamshire; Honorary Consul for Finland for Immingham, Grimsby and Hull and Deputy Lieutenant of the County of Lincolnshire.
- **Justin Atkin – Independent Non-Executive Director**
Justin is the UK and Ireland representative for the Port of Antwerp and an independent industry expert.
- **Steve Williams MBE – Managing Director, Executive Director**

Steve is employed by Portico and is responsible for the strategic direction of the company. He has over 30 years' experience in the port sector and is a full-time employee of Portico. Steve was awarded the MBE in the Queen's honours in 2020 for his work at Portico during the pandemic to maintain operations and ensure essential supplies continued to flow to supermarkets.

- **Richard Lewis – Operations Director, Executive Director**
Richard is employed by Portico and is responsible for the Health and Safety and the day to day running of Portico. Richard's career in maritime and shipping began in the merchant Navy where he served as a Deck Cadet to Chief Officer, sailing worldwide on ocean salvage vessels. He then moved to onshore operations, working as a General Manager at Geest Line for 30 years. He was previously Head of Operations at Portico.
- **Mark Webb – Chief Financial Officer, Non-Executive Director**
Mark is employed by the Council, as a Finance Manager and has been based at Portsmouth International Port since 2010. He heads up the finance team at Portico and brings a wealth of financial and commercial expertise to the company.

7.3 Historically there have been PCC Councillors on Portico's Board, consisting of a member from the Administration and a member from the main opposition. This principle of cross-party representation on Portico's Board will continue.

7.4 Portico employs its own Company Secretary, Shakira Powell, who is a professional in maritime law and a full-time employee of Portico.

7.5 Portico ensures that its directors, together with its wider workforce, maintain the necessary skills to discharge their responsibilities.

8. Integrated impact assessment

8.1 An integrated impact assessment is not required as the recommendation does not have a negative impact on any of the protected characteristics as described in the Equality Act 2010. The capital investment is in Portico business, and it is not for any service that could impact on customers from an equality perspective.

9. Legal implications

9.1 Article 107(1) of the Treaty on the Functioning of the European Union (TFEU), provides a general ban on state aid, that concept now being superseded by the UK leaving the European Union so now sits within the Subsidy Control Act that came into force on the 4th January 2023. The provision of support and or aid is assistance (in any form whatever) given by public bodies to selected undertakings (who are engaged in economic activity), which could potentially distort competition and affect trade between businesses within the UK and through trading upon an international basis. The principles of subsidy control are set out in Schedule 1 of the 2022 Act A-

G. The main one relevant to Portico is G which looks at who a subsidy can be dealt with in the sense of not amounting to a provision of support that would distort an internal or international market etc.

- 9.2 The Act requires decisions about the provision of support to have regard to the statutory guidance - see sec79(6) of the Subsidy Control Act.
- 9.3 Previously, economic transactions in the form of investment in a private undertaking carried out by a public body which do not confer an advantage on the undertaking, do not constitute aid if they are carried out in line with normal market conditions, and in accordance with so-called 'Market Economy Operator (MEO) Principle'. In order to satisfy the MEO Principle, the Council must assess whether, by making the proposed investment based on Portico's Business Plan, it will act as a private investor would, in similar circumstances. The measures in place and set out in this report seek to demonstrate that the Council adheres to the MEO principle in accordance with all previous advice. As a matter of good practice it would be advisable to receive expert advice on the continued adherence to the MEO principle and related subsidy control matters.
- 9.4 If the proposed loan investment in Portico is based on genuinely commercial terms, and the Council is investing in a way that a rational private investor would, then it is potentially not providing support that would engage a subsidy control consideration. To satisfy subsidy control principles the 2022 Act lays down the process that would need to be considered to establish that the Council's loan investment in Portico is on terms that would be acceptable to a genuine private investor. The aim of undertaking compliance with the Act is to maintain a position Portico would not be receiving an advantage from the Council that it would not have otherwise obtained on the market. The Council is continuing its previous "state aid compliant" practice in this regard.
- 9.5 Investment proposals relying on the MEO Principle justification should be supported by at least one independent report from a reputable source confirming that the terms and conditions would be acceptable to a market investor. The Council has commissioned an independent expert assessment of the proposed investment in Portico, which has confirmed that a private entity would provide such investment based upon Portico's Business Plan.
- 9.6 In addition to the above it is recommended that the proposed strategy and loan facilitation proposals together with the structuring of Portico (new companies and officers) be scrutinised by reference to independent legal review principally focussing upon establishing that the proposals of this report are fully compliant with current legislation.
- 9.7 It is considered likely that the MEO Principle, based on the proposals set out in this report, would be satisfied.
- 9.8 However, the Council must ensure that:

- Conditions are attached to the loan facility to enable it to check that the Business Plan is on track.
- It continually reviews the progress of the implementation of the Business Plan to check that it continues to present an attractive investment that a rational private investor in the Council's position would be prepared to make.
- It puts in place adequate regular reporting controls to facilitate such reviews.
- It regularly reviews its investment and re-visits the alternative options.

10. Director of Finance's comments

10.1 The financial implications associated with the options appraised are contained within the body and Exempt Appendix A of this report.

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Signed by:

Appendices:

Exempt Appendix A: Financial Review and Appraisal
Exempt Appendix B: Company Structure Summary

Background list of documents: Section 100D of the Local Government Act 1972

The following documents disclose facts or matters, which have been relied upon to a material extent by the author in preparing this report:

Title of document	Location

The recommendation(s) set out above were approved/ approved as amended/ deferred/ rejected by on

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Signed by: