

Welcome to our summer 2019 newsletter. We focus on demand and supply issues for business space across our region and review a selection of our recent projects.

## Business space defined

Business space is defined as **offices and industrial space (warehousing, logistics and workshops)**. We include **development land with (or the potential for) planning permission and allocated employment sites** in the local plan.

In planning terms, the definition of business space (B1, B2 and B8) remains unchanged since the Town and Country Planning (Use Classes) Order (as amended) 1987. However, the end product, predominantly driven by the impact of technology and how businesses operate, is ever changing.

Modern buildings are bigger, taller, more energy efficient and have a direct impact on how firms work.

## Business space demand

Historically, recording the take up of net business space was a reasonably good proxy for estimating future demand but given the increasing pace of business and economic change we are of the opinion it is no longer a reliable indicator.

Occupier requirements are increasingly difficult to determine as businesses have different needs and objectives, different building requirements, take time to engage with the market and are not always good at articulating to 'the market' what they want and when they need it. In addition, their financial and operational objectives are not always aligned to space usage ie there is usually a time lag and hence the need for lease flexibility.

Occupiers are always cost driven given the continuous focus on operating margins but the property market thinks in terms of rents / capital values / returns. There is a huge mismatch in approach.

All these factors do not help a developer seeking to build new business space given the time it takes to buy a site, secure planning and build. In fact, it is one of the reasons why a limited amount of new space is built in the regions where the economics are usually marginal ie capital value less build cost / risk = profit / loss). The risk of poor returns is high given the destructive



impact of the time value of money on the financial outcome. By definition, developers need to be strategic, analytical, take a long term view in order to maximise returns and have good timing.

Later in this newsletter we review two successful speculative new build schemes we are involved with – Glenmore Business Park and Ravenna Point.

In terms of this industrial space, occupiers focus on total occupancy costs, good access to main trunk roads, yard space for deliveries, internal heights / dimensions and long-term operational resilience. In addition, the sector is having to accommodate continued and competing demand from retailers seeking distribution units across the UK to satisfy ever changing retail buying habits.



## Business space demand continued

For office occupiers, square feet per person and cost per person are important metrics along with location and operational and financial flexibility. For re-location / acquisition projects we apply **the three L's – Lease, Location and Layout** – to get under the skin of the instruction. The debate around out of town or in town for office occupiers continues and is very personal to each situation and staff. Both have their pros and cons and it is of course important to look at the overall property costs.

For an office user, a simple equation can help identify key property cost drivers:

$$\text{Total property costs} = \text{Sq Ft per employee} * \text{Total property cost per employee} * \text{Total employees}$$

It warrants mentioning *We Work*, an American company that provides shared workspaces for technology start-up subculture communities and

services for entrepreneurs, freelancers, start-ups, small businesses and large enterprises. It was founded in 2010 and by January 2019 had a valuation of roughly US\$47 billion managing around 10,000,000 square feet worldwide. We Work have locked into untapped demand from established business communities seeking to use premium space on a very flexible basis.

On the financing side the own versus lease debate continues and is personal to each situation. Typically, SME's prefer to own but larger organisations prefer to rent and use their capital in the business rather than invest in commercial space and take the risk on the residual value of the property. Short leases of less than 5 years with built in flexibility driven by operational need are the norm given the general pace of business change. Also, as all property leases are now recorded 'on balance sheet' corporate entities are very focused on limiting their exposure and short leases are one way of doing this.

## Business space supply

Earlier this year, we undertook desk top research to identify the supply of 'available' business space on the market within a 25 mile radius of our office in Chichester. The results are set out below and some interesting conclusions can be drawn.

We classify supply in three different categories:

- **Grade A** - new / quality retrofit.
- **Grade B** - very good / general refurbished space.
- **Grade C** - everything else.

OFFICE	sq ft	%	Average quoting face rent per sq ft
Grade A	57,844	54	15.50
Grade B	49,040	46	13.00
Grade C	n/a	0	n/a
<b>TOTAL</b>	<b>106,884</b>		

The quantum of 'Grade A' space is not high and could be linked to the fact that average office face rents across the region are not high enough to encourage a developer to build out new office space

speculatively - it is too risky with a capped upside. We would advise that average face rents for new space of at least £20 psf to encourage development.

INDUSTRIAL	sq ft	%	Average quoting face rent per sq ft
Grade A	340,523	21	9.50
Grade B	1,126,935	70	8.00
Grade C	126,121	8	6.00
<b>TOTAL</b>	<b>1,593,679</b>		

Prime industrial rents across the region have dramatically increased from +/- £7.50 psf to +/- £9.50 psf over the last two years but we feel they have probably peaked for the immediate future as the level of growth is not sustainable as occupiers are increasingly cost conscious and are delaying property decisions given the general uncertainty in the economy.

Capital values are a function of these rents and it is not uncommon to see initial yields for prime new space let on bankable lease across our region in the range of +/- 7% - a good comparative income return even if rental growth and yield compression is limited.



# Business space **supply** continued

In terms of the potential for 'new' supply 57 hectares of land over 5 sites is outlined for commercial development in the Chichester local plan. These sites are summarised below.

Site	Hectares	Use
White House Farm	6	B1
Glenmore Bus Park	4	B1 / B2
Southern Gateway	12	B1a B1b
Manor Farm	33	B1b/ B1c B2 / B8
Chichester Bus Park	2.4	B1 / B8
<b>TOTAL</b>	<b>57.4</b>	

More specifically, the Chichester draft Local Plan recommends a total net additional floor space of 145,835 sqm's (1.570m sq ft) is provided over the period 2016-2035. Split between 49,419 sqm of B1a/b, 34,561 sqm of B1c/B2 and 61,855 sqm of B8.

This is a staggering amount given the space already on the market and we question whether it will actually happen given the statistics set out below.

- The total population of Chichester District is only 120,200, a growth of 17.36% since 1995, with average growth of 0.75% per annum.
- 56.27% of the local working population is in the age range of 16-64 which below the national level of 63.1%. This is in contrast to those over the age of 65 at 27.01% compared to the national level of 18%.
- By 2035 those of working age are expected to account for only half of Chichester's population, whilst the number of people aged 65 and over is expected to account for 35%.

The delivery of new space on the sites set out above implies new businesses being attracted to the Chichester District as well as developers taking the risk and building out in anticipation of this demand.

**We touch on this point later on in this newsletter as we are involved with a visionary scheme for the Southern Gateway called *The Forum*. This scheme will position Chichester as a 'go to' location on the south coast for business, education and leisure. The outcome would be cutting edge and innovative - it is the catalyst for positive change across The District and in particular central Chichester.**





## Recent projects

Commercial property transactions, large or small, are different, time consuming, potentially complex and require a legal contract.

**An experienced and rigorous approach** is needed to add value rather than saddle the business with an onerous liability.

Recently, we were instructed to assist clients on the acquisition of business space. These organisations did not have the internal resources or expertise to source and acquire the required space, were not used to interfacing with the commercial property market, generally too busy with their 'day' jobs and were happy to outsource to a property adviser.

## Tennyson Insurance (part of the Zurich Group)

Two years before a lease expiry of its existing office facility Tennyson Insurance Ltd appointed us to assist them with the acquisition of up to 10,000 sq ft of office space in and around Chichester. The senior management team were open minded about the outcome but required a rigorous process to secure best value.

**Stage 1** - We followed a structured approach by agreeing a detailed brief of requirements with Tennyson and then undertaking a formal and discrete search on availability in order to preserve a negotiating position.

**Stage 2** - A range of workable options were identified that matched the brief. We requested additional information on some of the options to allow appropriate for discounted cash flows to identify the NPV of the likely cost of each option. The cash flows included occupancy costs as well as capex and dual running costs. We also identified qualitative issues with each option. The results were presented to the client - two options floated to the top – one was cheaper but the business had concerns about the location. The other was more expensive, required a full refurbishment but



was generally better suited the business objectives / long term needs.

**Stage 3** - The Board made a directional decision to progress the riskier refurbishment option, commercial terms were agreed and the legal documents were drafted (agreement to lease / occupational lease / building specification) and signed.

**Stage 4** - As the property was listed, planning permission was required for the refurbishment works. In addition, a detailed specification was agreed between the parties. During the works, Tennyson moved into temporary space on site at nil incremental cost in order to limit double occupancy costs during the works. The works will complete late 2019.

## QB Technology



**An innovative modular construction company needed a large factory, funding and staff to**

**implement their ambitious business plan. Our role was to help the business source and secure the property on a leasehold basis.**

The 'perfect' building was identified – a self-contained 70,000 sq ft production facility with modern office space on a 1.5 acre site with direct access onto a main trunk road. However, the space was already occupied by a global occupier, SSD Drives Ltd (a division of Parker Hannifin Corporation), via an onerous FR&I occupational lease. In addition, the property had fallen into disrepair.

Discussions started and it became evident that the majority of the space was actually surplus to requirements and only a small part was required by SSD Drives.

Negotiations commenced, building due diligence was undertaken and detailed terms were agreed between the parties subject to approval by the freeholder and various guarantors. As part of these terms QB's responsibility for the ongoing up keep of the fabric, M&E and exterior space, internal repairing obligations, service charge contributions and of course future dilapidations were mitigated to limit unexpected costs over the duration of their occupation.

In this instance, the use / resilience of the space was of paramount importance given the proposed use as well as the running costs including the rent.

QB Technology are now in occupation and we are working with them on new business opportunities.



## Chichester Festival Theatre

We were instructed to source and acquire space to allow the Chichester Festival Theatre accommodate visiting productions. A key objective was to own space close to the Theatre with the sole purpose of making significant savings against the baseline position of renting space in various locations around Chichester on an inflexible basis.

We acquired a building from a developer who in turn secured the required planning consent and refurbished the existing building on a prime part of the site to The Theatre's requirements. The transaction involved market appraisals and financial analysis, general due diligence and agreeing detailed terms.

The Chichester Festival Theatre acquired an asset that will save the business money, generate a good return



on the initial outlay given the savings and in theory should go up in value. In return, the developer received a fair risk adjusted profit as well as the sale kick starting the balance of new development on the site.

## St Cross Homes

Back in 2014, a residential developer missed out acquiring the freehold interest in an office building we were marketing on a 'For Sale' basis in central Chichester – a 35,000 sq ft office building let to the Secretary of State on a long lease. The building sold to a property company given the nature of the long lease.



At the end of 2018, this residential developer instructed us to try and buy back the building even though it was not on the market – their sole objective being to convert the 1st and 2nd floors to residential via permitted development rights that currently apply in respect of the change of use of premises from a B1(a) office use to C3 residential use.

We approached the freeholder and heads of terms were agreed to buy with cash on an unconditional basis. A prior approval notice was submitted to Chichester District Council and the purchase completed prior to Easter 2019.

The conversion is expected to commence later this year (2019) with completion of 26 residential units in 2020. The commercial space to be retained on the ground floor and let in the open market.

## Paragon Skills



During 2018, we were instructed by Paragon Education & Skills Limited to assist the business mitigate the exposure on a 30,000 sq ft purpose built facility

occupied on a long leasehold basis in Bournemouth.

The total occupancy cost exposure on the lease until lease expiry was £4.2m and more than the actual capital value of the building. Doing nothing was not an effective use of resources.

We identified the likely exit options for the leasehold interest, provided detailed financial analysis on a discounted cash flow basis and provided recommendations on next steps.

Five options were analysed : mothballing, assigning, subletting, surrender and buying in the freehold with a sale, with vacant possession at a later date. Each had pros and cons and different financial outcomes.

A report was provided to The Board who decided to continue with the operations on site given the extent of the property exit costs and the risks around dealing with a surplus building in an off-pitch location.



## The Forum



Late 2018, we were asked by Gateway Plus to promote their scheme which focused on the re-generation of Chichester's Southern Gateway.

Our role was to work with Gateway Plus to help deliver their masterplan called The Forum. Key objectives were:

- Create an exemplary destination to attract business and generate significant 'new' employment opportunities for the region.
- Position locality and Chichester as a 'go to' destination on the South Coast for progressive SME's.
- Encourage local talent to stay local and secure local employment.
- Encourage more tourism and leisure activities in the centre of Chichester.
- Link the Southern Gateway to central and Northern Chichester via inviting civic space.
- Upgrade the railway station, close the railway crossings and build an underpass.
- Create a direct rail link from Chichester to Bognor Regis.



- Create a new transport hub to limit congestion.

At the heart of the Gateway Plus masterplan are a conference centre, an international hotel with support space, some complementary residential space aimed at young professionals working locally and public realm. It has been called The Forum.

And  
finally

**We are agents on two new build industrial schemes in Chichester. Glenmore Business Park - owned and built by The Glenmore Group – and Ravenna Point - owned and built by Chichester District Council.**

Both are very different schemes aimed at different occupiers either looking to buy or lease new commercial space.

The landowners decided to build speculatively, take the market / specific risk and the financial reward.

## Glenmore Business Park



**180,000 sq ft speculative scheme on 10.5 acre site on the A27 just outside Chichester. Built out in two phases**

**offering B1(c), B2 and B8 units ranging from 1,000 sq ft to 23,000 sq ft. Available on a freehold or leasehold basis and aimed at owner occupiers / investors.**

Phase 1 commenced in 2016 and by practical completion virtually all the units were sold. Phase 2 commenced in 2017 with practical completion early 2019 – once again by this date virtually all the units had sold. Buyers were predominantly owner occupiers with more investors in Phase 2.

This scheme has set a new benchmark for capital values for the locality ranging from £130 to £160 psf across ground floor and the mezzanine space.

## Ravenna Point



**Ravenna Point is a 16,360 sq ft speculative scheme built on an acre site on Terminus Road. Planning permission for B2 / B8 / 40% trade counter plus additional mezzanine space (7,300 sq ft) that could be built out by future tenants or Chichester District Council.**

The development completed in early 2019 and we secured a letting of units 5 and 6 (5,000 sq ft) prior to practical completion. Marketing continues for the rest of the space and we expect more lettings during 2019 given the quality of the space, the generous parking and the location.

### Next steps

We are a discrete, flexible and rigorous resource that helps clients maximise returns from the capital invested in their business space.

You may be an occupier where your business is going through a period of change, looking to move and acquire new space, downsizing and disposing of surplus space, has a lease expiry, is expanding or just wants to run a slide rule over its existing space to make sure it is maximising value.

Alternatively, you may be an investor / developer looking to secure a specific site, negotiate a transaction with a tenant, resolve a planning problem or just want to dispose of some business space in the open market.

We have a good track record adding value, avoiding conflicts of interest and resourcing projects in a professional manner.

Why not get in touch to see how we can help your business marry up its spatial needs with its business objectives.

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