

Cabinet

13th March 2024

**New Business Units
South Church Enterprise Park, Bishop
Auckland**



Ordinary Decision

Report of Corporate Management Team

Amy Harhoff, Corporate Director of Regeneration, Economy, and Growth

**Cllr James Rowlandson, Cabinet Portfolio Holder for Resources,
Investment and Assets**

Electoral division(s) affected: Bishop Auckland

Purpose of the Report

- 1 To seek approval to progress the development of speculative business units on land owned by the council at South Church Enterprise Park, Bishop Auckland, as part of the Stronger Towns Programme.

Executive Summary

- 2 County Durham has a shortage of new industrial units which is restricting the growth of new and existing local companies wanting to set up or grow a business.
- 3 The Council Plan 2023 - 2027 includes the ambition “to create more and better jobs in an inclusive green economy” by supporting businesses emerging from the pandemic and by developing a pipeline of projects and investment plans at major employment sites across the county.
- 4 County Durham’s Inclusive Economic Strategy (IES) sets a vision for the area’s economy up to 2035 that includes developing employment land for improved infrastructure, providing better facilities and opportunities for businesses in the area.
- 5 There is an opportunity for the council to directly develop additional much-needed business units at South Church Enterprise Park, Bishop Auckland. This could see some 45,000 sq ft of units built for new and young small businesses needing space from 1,000 to 2,000 sq ft. The local enterprise agency would provide wrap around support for the new businesses as part of a wider Bishop Auckland scheme.

- 6 The scheme of new units has been designed to RIBA Stage 2 Concept Design under the management of the council's Construction Consultancy Service with an estimated total capital cost of £8.5 million. Of this, £1.5 million would be met through a grant from the Stronger Towns Fund, £1.8 million from the UK Shared Prosperity Fund (UKSPF) (approved in principle) with the council requested to fund the £5.2 million balance on a self-financing basis and with a projected return of 12.69%. To meet the timescales associated with UKSPF funding the £1.8 million must be spent by March 2025, which will require the project to be taken out to tender in April 2024, and to award the tender the full funding package as outlined in this report must be in place.
- 7 The RIBA 3 Detailed Design Stage is currently being undertaken and due imminently, in order to ensure the appointment of a design and build construction partner by August 2024, works to commence on-site in December 2024 and to complete by August 2025.
- 8 The new units would be owned by the council and marketed and managed by Business Durham as part of the wider commercial portfolio. Once occupied, the units could support over 20 new or young businesses and over 110 new jobs.

Recommendations

- 9 It is recommended to:
 - (a) Agree to progress the scheme of new business units, apply for all statutory approvals, and go out to competitive tender for a construction partner.
 - (b) Delegate authority to the Corporate Directors of Regeneration, Economy and Growth and Resources in consultation with the Portfolio Holder for Resources, Investment and Assets, to enter into the construction contract should it be achievable within the council funding envelope set out within this report.

Background

- 10 County Durham has a shortage of new industrial units which is restricting the growth of new and existing local companies wanting to set up or grow a business. Demand has consistently outstripped supply but with market rents too low to attract direct development from the private sector, then support is needed from the public sector to encourage new development in the County.
- 11 The Council Plan 2023 - 2027¹ includes the ambition “to create more and better jobs in an inclusive green economy” by supporting businesses emerging from the pandemic and by developing a pipeline of projects and investment plans at major employment sites across the county.
- 12 County Durham’s Inclusive Economic Strategy sets a vision for the area’s economy up to 2035 that includes developing employment land for improved infrastructure, providing better facilities and opportunities for businesses in the area.²
- 13 A market research study from Lambert Smith Hampton³ commissioned by Business Durham in July 2022 states that some industrial estates with good access to the A1(M) and A19, have seen some speculative developments of industrial units whereas at locations such as South Church, rents are lower and speculative private sector industrial development has generally relied on public sector gap funding or direct development.
- 14 The report concludes that in Bishop Auckland, there is an acute shortage of new industrial property and pent-up demand that would be satisfied by this scheme at South Church. There is a need to consider public sector support to bring forward investment in new industrial units, and also to provide a support package to help create and sustain the growth of new and young businesses.

South Church Enterprise Park, Bishop Auckland

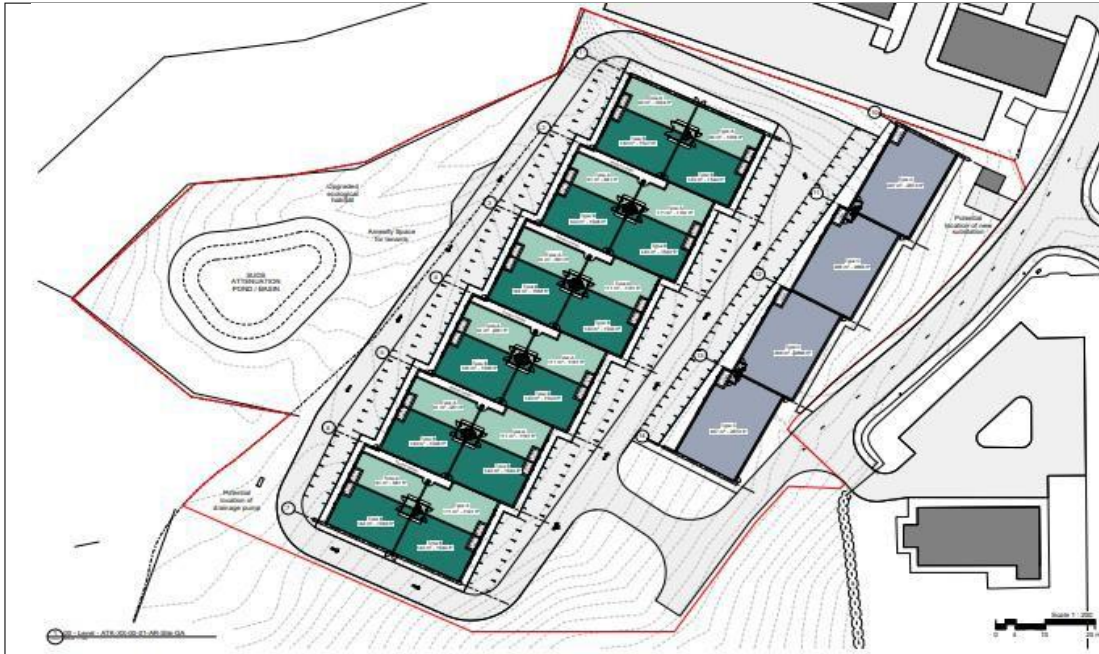
- 15 An opportunity to develop additional small business units has come forward on land owned by the council at South Church Enterprise Park, Bishop Auckland, where demand remains high but where there is a shortage of small industrial units, similar to other areas across the County.
- 16 The site owned by the council could provide some 45,000 sq ft of units built for new and young small businesses needing space from 1,000 to 2,000 sq ft. The local enterprise agency would provide wrap around support for the new businesses as part of a wider Bishop Auckland scheme.

¹ Durham County Council Plan page 26

² County Durham Inclusive Economic Strategy 2023

³ Property Market Research and Viability Assessment Lambert Smith Hampton July 2022

- 17 As shown below, a design to RIBA Stage 2 has been produced showing up to 28 units ranging from 1,000 to 2,000 sq ft. The total capital cost is estimated at £8.5 million as of Q3 2024:



- 18 The scheme has been awarded up to £1.5 million from the Bishop Auckland Stronger Towns Fund towards the build costs. The scheme forms a key part of the programme alongside the enterprise support package to be delivered by the South Durham Enterprise Agency (£0.15 million).
- 19 In addition, the scheme has been awarded in principle, up to £1.8 million from the UK Shared Prosperity Fund (UKSPF). This would leave a balance of £5.2 million to be funded by the council on a self-financing basis, with the rental income repaying the upfront investment over a 35-year period.
- 20 The scheme is continuing to progress with the RIBA 3 Detailed Design due to be completed imminently. The initial development cost of the project is being funded from secured Stronger Towns Fund monies. This approach has been adopted to ensure the scheme is 'oven ready' so that it can progress in a timely manner when funding and budgets are secured. In Spring 2024 the tender needs to be issued in order to meet UKSPF spend deadlines in later months of delivery. To award the tender the full funding package needs to be in place.
- 21 The Head of Corporate Property and Land has concluded that the project will be designed and built externally, project managed by the in-house Construction Consultancy Service on behalf of Business Durham.

- 22 The units could support over 20 new or young businesses and over 110 new jobs. The new units would attract a wide variety of businesses, from small manufacturing to industrial and professional services, and with a range of sizes, provide a growing business the opportunity to move into the larger units within the estate.
- 23 The units would be owned by the council, marketed, and managed by Business Durham with target rents from £9.00 to £10.00 sq ft. which accords with discussions held between Business Durham and other agents in the region. Tenants would take on an internal repair only lease of at least three years from the council.
- 24 The remainder of the site could also allow a further development of some 40,000 sq ft of business space with strong interest already established by local companies wanting to self-build. This could provide a capital receipt to the council of approximately £0.25 million and create up to a further 100 new jobs in the area.
- 25 It is expected that all units will be let within the first two years following practical completion, although the financial modelling detailed later in the report is based upon more prudent assumptions.
- 26 The project will contribute to the Inclusive Economy Strategy for County Durham as follows:
- (i) More Jobs: The project will support the creation of new businesses and the growth of existing businesses in the Bishop Auckland area.
 - (ii) Better Jobs: the project will provide much needed modern floorspace supporting growing businesses looking to recruit additional personnel from the wider area of Bishop Auckland.
 - (iii) Inclusive: the project will include an enterprise support programme available to all residents across the county looking to set up a new business.
 - (iv) Green: the business units will be built to BREEAM very good and include where affordable EV charging, PV panels, reduced carbon embodied materials and no gas supply, supporting the journey to net zero carbon for County Durham.
 - (v) People – the project will provide enterprise support and training to affect new business growth for the residents of County Durham.
 - (vi) Productivity – the project will provide modern, energy efficient buildings supporting business growth and higher levels of productivity in businesses across the area.

- (vii) Places – the project will extend the existing enterprise park with new and improved buildings and infrastructure, providing better facilities and opportunities for business in the area.
- (viii) Promotion – the project will provide opportunities for growing businesses, residents looking to set up a new business.
- (ix) Planet – the project will support growing businesses operating in modern, energy efficient premises, supporting the ambitions of net zero carbon emissions in County Durham by 2045.

27 The project will help create and sustain jobs for local people, inspire entrepreneurial culture within the local community and contribute to the overall economic development of the Bishop Auckland area.

Financial Analysis

28 The total capital cost of the scheme is estimated at £8.5 million funded as follows:

Stronger Towns Fund	£1.50 million
UKSPF	£1.80 million
DCC	£5.20 million
Total Capital Cost	£8.50 million

29 A detailed financial analysis of the project is shown in Appendix 2 with a summary below:

South Church Enterprise Park - 14.12.2023 - 4.5% option	
	1
	Capital Cost £8.5million
Capital Build Expenditure	£8,500,000
Grant	(£3,300,000)
Capital Finance required	£5,200,000
Financing Years	35
Capital Interest Rate	4.5%
Net Return £ (35 year)	£1,322,585
Net Return % (35 year)	12.69%

Gross Rental Income	£15,857,813
Voids (Rents)	(£2,501,103)
Net Rental Income	£13,356,710
Financing Charge (Interest + MRP)	(£10,423,222)
Management Fee/ Sinking Fund	(£772,486)
Void Costs	(£838,419)
Other	£0
Net Revenue Surplus / (Deficit)	£1,322,585
% Return	12.69%
Assumptions;	sq ft
Total sq ft - Unit Size 981-1191 sq ft	12,868
Total sq ft - Unit Size 1540-1548 sq ft	18,539
Total sq ft - Unit Size 2866-2873 sq ft	11,478
Total Net sq ft for rent - Total	42,885
	No. Units
Total units at 981-1191 sq ft	12
Total units at 1,540-1548 sq ft	12
Total units at 2866-2873 sq ft	4
Total units	28
Rent 981-1191 sq ft	£10.00
Rent 1540-1548 sq ft	£9.50
Rent 2866-2873 sq ft	£9.00
Rent uplift y1-15	1.00%
Rent uplift y16-25	0.50%
Rent uplift y26-35	0.00%
Management allowance	5.00%
Voids (after year 3)	15.00%
Asset Life (years)	35
-	-
-	-
<u>Occupancy Assumptions y1 -3</u>	-
Year 1	50%
Year 2	75%
Year 3	100%
Year 4 onwards	85%

- 30 The business case developed applies a current interest rate on debt of 4.5% resulting in a net return of 12.69% and a net surplus of £1.32 million over 35 years but with a cashflow deficit until year 10 peaking at £216,500 in year 2.
- 31 The completed scheme of 45,000 sq ft would likely generate an estimated £250,000 annual business rates for the council.

Programme

- 32 The current programme has the following milestones:

- (i) Funding Approval: March 2024
- (ii) Planning Approval: June 2024
- (iii) Out to tender: May 2024
- (iv) Contractor appointed: August 2024.
- (v) Start on site: December 2024
- (vi) Construction completes: August 2025

Risk Assessment

- 33 A number of risks need to be considered in relation to the council agreeing to finance the development and to take on responsibility for future tenancies. Key risks are identified below with mitigation:
- (a) **Capital build cost** – the fully tendered cost could be higher than the forecast £8.5 million although the intention is to secure a Guaranteed Maximum Price (GMP) within the available budget. Should the GMP push the total scheme costs beyond the agreed council self-financing envelope of investment then further external funding support would be sought to bridge the gap, or consideration given to bring a further business case to increase council funding.
 - (b) **Attracting tenants** – if the council through Business Durham is not able to attract tenants at the rate outlined in the financial appraisal, this could result in longer voids and reduce rental income to the council, resulting in increased costs and a smaller overall return. However, the units would be marketed and managed by Business Durham who have current occupancy levels in excess of 95% on stock of a similar size in the immediate area.
 - (c) **Rental levels** – the council may not be able to secure rental levels of an average £9.50 sq. ft. for the units as forecast and the annual increases from that level may not materialise. A sensitivity analysis shows that a drop in average rent of £1 sq ft would show a reduced surplus of £63k which is in effect breakeven with a surplus of 0.61%.

Should further assurance be required a formal valuation could be carried out, although it should be noted that Business Durham have strong market knowledge as they manage and market 190 industrial units across 18 industrial estates in the county, holding one of the largest portfolios of properties of this type across the region.

- (d) **Debt management** – The financial model shows a positive return of £1.3 million over 35 years but with a cumulative deficit until year 10, which peaks at £0.216 million in year 2. Any loss will be covered by the Commercial Reserve for the first two years of operation, after which any impact will be managed within the Regeneration, Economy, and Growth cash limit budget.
- (e) **Development Quality** – the current scheme has been designed to encompass the low carbon ambitions of the council and the target of achieving BREEAM Very Good.
- (f) **Building Maintenance** – there is a provision in the financial forecasts of around £20,000 per annum to support on-going repairs and maintenance but this does not account for the external repairs and maintenance budget which currently sits with Corporate Property and Land, and this budget is under significant pressures. This is not a specific issue relating to this scheme, and the self-financing modelling applied in this report is consistent with Durham County Council's methodology and how previous schemes have been assessed. It should however be noted that there is a future review proposed on how capitalised maintenance budgets are funded and administered.
- (g) **Stronger Towns Fund** – the scheme is the subject of approved grant of £1.5 million that needs to be claimed by the end of March 2026 which would be within the current programme.
- (h) **UKSPF** – the scheme is also subject to a grant of £1.8 million from UKSPF which must be claimed by the end of March 2025 which would be within the current programme.

Conclusion

- 34 The development at South Church would provide some 45,000 sq ft of much needed floorspace for new businesses in the area and would support the broader economic objectives of the council and its partners.
- 35 The upfront investment of £5.2 million from the council is significant and not without risk but is on a self-financing basis and repaid through rental income over an acceptable payback period. All market analysis shows high demand, and with the marketing and management of the units coordinated by Business Durham on behalf of the council, measures would be in place to mitigate the risk.
- 36 The case to bring forward speculative industrial development from an economic development perspective is stronger than ever as although rental yields are improving, there remains a gap between build costs and capital

values that deters private investment, especially for smaller units for new and young businesses.

Background papers

None

Other useful documents

LSH Demand Study July 2022

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Appendix 1: Implications

Legal Implications

The council owns the land at South Church with no need for further acquisitions.

The council would need to enter into grant funding agreements with UKSPF and the Stronger Towns Fund.

Finance

The report provides the financial analysis for the scheme.

Consultation

None.

Equality and Diversity / Public Sector Equality Duty

None.

Human Rights

None.

Crime and Disorder

None

Staffing

Business Durham already manage industrial units and will absorb the additional resource requirement.

Accommodation

None.

Risk

The risks and possible mitigations are detailed in the report.

Procurement

The scheme would be project managed internally and procured through existing frameworks.
