

Enterprise M3 Board meeting

26 July 2016

Commercial Property Market Study – Item 8

The Enterprise M3 Board is asked to:

ENDORSE the final report of the Enterprise M3 Commercial Property Market Study and note that it will be officially launched at the Enterprise M3 infrastructure event on 19 September 2016.

1. Background

1.1 The Enterprise M3 Land and Property Action Group have commissioned Regeneris Consulting and Aspinall Verdi to refresh its Commercial Property Market Study (2013). The main aims of this have been to:

- Provide the LEP with a robust evidence base on commercial property market conditions in different parts of the EM3 corridor;
- Analyse recent trends in the LEP's priority growth sectors, and understand the key location and property requirements of these sectors;
- Identify the key opportunities and challenges facing the commercial property market in different parts of the LEP area, and
- Make recommendations on how the LEP and its partners can use their funding and influence to address the strategic opportunities and challenges identified in the report, and support the growth of key sectors.

2. Dissemination of the Final Report

2.1 The final report will be available to download from the Enterprise M3 website at <https://www.enterprisem3.org.uk/commercial-property-market-study> and a copy of the executive study is included with this paper.

2.2 The recommendations of the draft report were considered by the Enterprise M3 Board at the meeting on 24 May 2016 and the comments raised have been incorporated into the final report. The draft report was well received and its content has been checked with Local Authority Economic Development and Planning Officers.

2.3 Once endorsed by the Board it is suggested that the link to the final report and a copy of the executive summary is circulated to the following groups who have overseen or contributed to this research:

- The Enterprise M3 Land & Property, Transport and Enterprise & Innovation Groups
- Local Authority Chief Executives, Economic Development Officers and Planning Officers
- Commercial Property Market Agents who were invited to and/or attended the Breakfast Workshops

2.4 The report will be officially launched at the Enterprise M3 infrastructure event on 19 September. This will include a presentation from Oliver Chapman, Associate Director, Regeneris Consulting. Following the official launch the key messages of the report will be disseminated to a wider number of groups including the Chambers of Commerce, Construction and Property

Forums, RICS and RIBA. The Enterprise M3 Land and Property Action Group will oversee the dissemination of the key messages.

- 2.5 The report will also form a key part of the information available at MIPIM UK which is the UK's largest exhibition and conference for property professionals. Enterprise M3 will be attending MIPIM as part of the Greater Thames Valley LEP Group and Surrey County Council, under the banner of Invest in Surrey, will have a stand at the exhibition. Hampshire County Council are planning some focused developer events targeting the property profession in London later in the year. These events will showcase opportunities for investment in the LEP area and hence will draw on the evidence base in the Commercial Property Market Study report.

3. Development of an Action Plan

- 3.1. The Land and Property Action Group are now completing an action plan to take forward the recommendations of the report. The action plan will include:

- Drawing on evidence in the report to identify priorities in the next draft of the Strategic Economic Plan – for example the study has found a shortage of industrial space and land with development potential. The shortage of industrial sites should be a priority in the next draft of the SEP.
- Drawing on evidence in the report to support the bid for funding for projects in the Local Growth Fund and identify opportunities for future LEP investments – for example where there are prohibitive site remediation costs on brownfield sites a public sector grant could be used to overcome the financial gap. The report has already proved invaluable in assessing EOI proposals for Growth Deal 3.
- Working with neighbouring LEPs to undertake further research on some of the issues identified – for example there is a need to work closely with the Solent LEP on their current review on logistics to build a clear picture on the undersupply of industrial sites.
- Working with local authorities as they prepare their local plans and updates – draw on evidence of the current supply and demand for office and industrial sites to support or influence strategies for the release of more land for commercial development. Several Local Authorities have indicated how useful the report will be as they undertake Employment Land Reviews.
- Improving information sharing between the LEP and local authorities through provision of a consistent set of indicators and providing information on local business trends and characteristics.
- Developing a better system for monitoring inward investment inquiries received for the LEP area to provide detailed intelligence on the nature of demand from investors.
- Working with Invest in Hampshire and Invest in Surrey to ensure that both are focused on the opportunities from London relocations in the next few years and where there are shared sectors joint sector propositions are developed.
- Reviewing the impact of permitted development rights and lobbying Government if necessary.
- Providing expertise to local authorities on the use of their own assets.

- 3.2 The Land and Property Action Group will be giving presentation to and working closely with the Enterprise and Innovation and Transport Action Groups in taking forward these actions through joint strategy planning and case making. They will also be monitoring the action plan to ensure the recommendations of the report are taken forward.

Name of Project Manager: Nikki Nicholson

Date of Report: 18th July 2016

Enterprise M3 Commercial Property Market Study

Executive Summary

Purpose of Study

- i. Regeneris Consulting was commissioned by the Enterprise M3 Local Enterprise Partnership (LEP) to update its Commercial Property Market Study which was last published in 2013. The study needed to address the following key questions:
- 1) Are the market areas set out in the 2013 report still valid?
 - 2) What is the availability, type and demand for commercial property in each market area and across the Enterprise M3 area? How can this be measured and monitored on an ongoing basis by Enterprise M3?
 - 3) What are the key opportunities and challenges in each market area and across the Enterprise M3 area?
 - 4) How can the LEP and its partners address the opportunities and challenges identified in each market area and across the Enterprise M3 area?
- ii. Given the sector and spatial focus of the Strategic Economic Plan (SEP), the study also needed to look at how the commercial property market is affecting the performance of key towns, and provide a review of the commercial property requirements of the LEP's four priority sectors; aerospace and defence, ICT & digital, pharmaceuticals and professional and financial services.

Market Areas

- iii. We have made two changes to the market areas from the 2013 study, shown in red in the figure below:
- **Central Hampshire divided in to Winchester and East Hampshire market areas.** Winchester is an office based economy whose strategic assets are its links to Southampton, Basingstoke and London. East Hampshire is mainly an industrial market, with strong links to Portsmouth, Guildford and the Blackwater Valley. This was agreed with local commercial agents and the councils.
 - **Guildford and Woking divided in to separate market areas.** Although the two towns have similar strategic assets and industries, commercial agents felt there was a clear difference in demand between Guildford and Woking which meant Guildford attracts much higher rents. The difference between the two towns was large enough for them to state that increasing supply in Woking could not make up for a shortfall of office space in Guildford. Therefore the two should be treated as distinct market areas.

Figure 1 Revised Market Areas (changed in red)



Source Regeneris Consulting

Needs of Priority Sectors

- iv. Of the four priority sectors, ICT and digital and professional and financial services are by far the largest in Enterprise M3, accounting for 28,000 businesses and 124,000 jobs (compared to only 460 businesses and 13,000 jobs in the other two sectors). These two sectors have been the major drivers of growth of Enterprise M3's economy, creating nearly 8,000 new jobs in the past five years. They have therefore had a major influence on recent trends in the commercial property market.
- v. Both sectors have very diverse property requirements, but there are a number of recurring themes. The key requirements are summarised below.

ICT and Digital

- **Flexible workspace:** a particular issue for digital start-ups, which are reluctant to commit to longer term leases because of the risk of the business failing. Co-working environments offering easy-in, easy-out accommodation also provide a space for these business to interact, collaborate, innovate and secure new business opportunities.
- **Town centre locations:** these offer a number of advantages for digital firms, including access to a young and highly skilled workforce who increasingly choose to live in urban locations and have lower rates of car ownership. Town centre locations also offer proximity to other businesses for networking and collaboration.¹

¹ Although town centres are highlighted here, any sites and locations offering good access to public transport (particularly rail connections) are likely to be at an advantage.

- **Superfast broadband:** this is now a core requirement for most sectors, but particularly the ICT/digital sector which is dependent on high upstream and downstream bandwidth for sharing files with clients and collaborators.

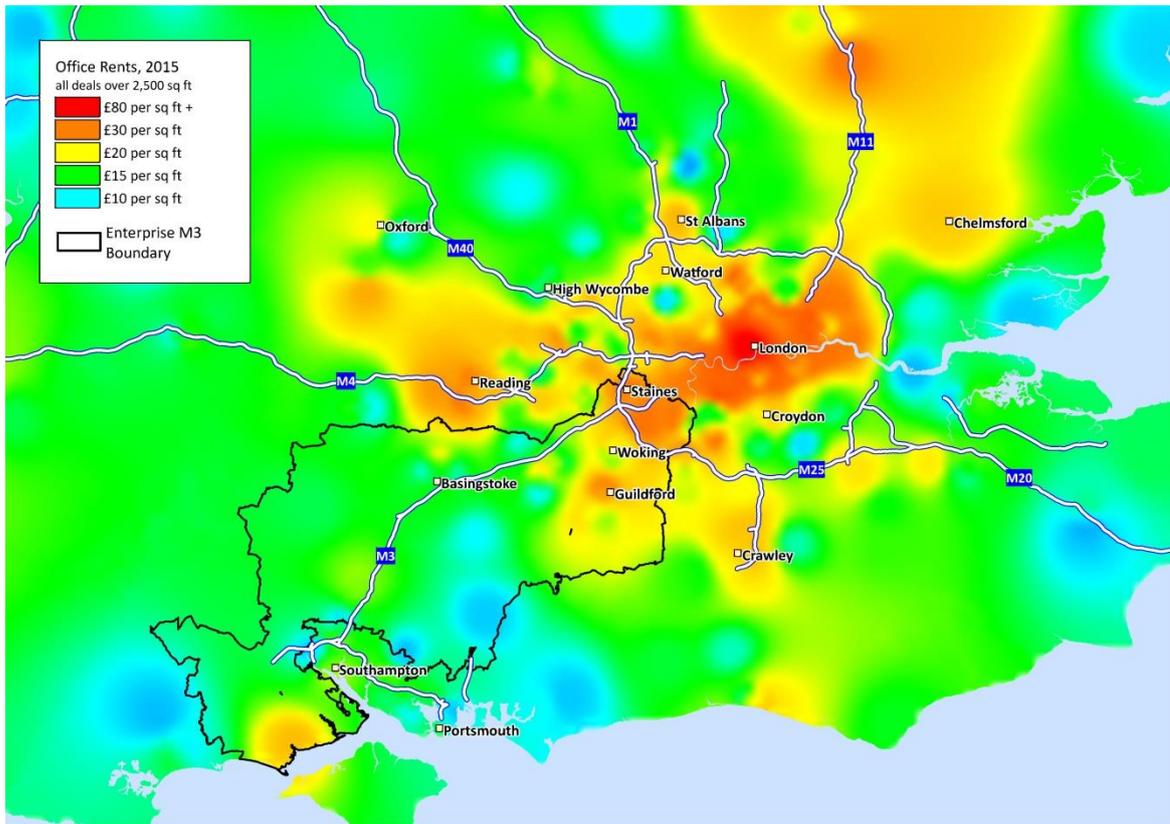
Professional and Financial Services

- **Access to London and Heathrow:** this is one of the main reasons why head offices and other large scale professional and financial services firms choose to locate in Enterprise M3. Connections to central London will grow in importance as more and more London based firms look to relocate parts of their operations due to high property costs.
- **Town centre locations:** like digital, this sector has seen a growing trend toward town centre locations because of the importance of attracting highly skilled workers.
- **High quality business parks and car parking ratios.** Travelling by car remains by far the most popular means of commuting in Enterprise M3. There is therefore still a major role for high quality business parks offering good leisure and retail amenities and high car parking ratios.

Office Market

- vi. Recent growth in office based sectors (particularly digital and professional services) has driven a strong increase in demand for office space in Enterprise M3. Take up of office space in 2015 was the highest it has been since before the economic downturn. Although a large number of these deals have been for smaller floorplates, it is the increase in larger office deals that has driven the strong recent performance.
- vii. The vast majority of these deals have been in the north east of the LEP, which are closest to London. This includes Woking, Guildford and Blackwater Valley, but particularly Upper M3, where a recovery in rental values has encouraged the development of new Grade A office space. This is increasingly a core requirement of most large investors and has seen the Upper M3 area attract a number of high profile HQs in the digital and professional services sectors.

Figure 2 Office Rental Values per sq ft, 2015



Source EGI

- viii. This pattern of rental values has resulted in quite an uneven performance in Enterprise M3's commercial property market, which is causing a number of quite diverse challenges across the LEP area.
- In **Basingstoke and Andover** and large parts of the **Blackwater Valley**, the challenge is an oversupply of poor quality, second hand space which is depressing rental values and discouraging investors from building new, high quality offices. Both areas are therefore losing out on investment to towns on the M4 corridor which have seen significant investment in high quality stock.
 - Both **Guildford** and **Winchester** have attractive town centres which have been in strong demand. The challenge here is a shortage of office space and sites in the town centre which is acting as a constraint on investment. This could be addressed in Winchester through the Station Approach development but remains a concern in Guildford.
 - **Woking** and **Upper M3** are both areas in high demand, but the good supply of sites in both locations means that the market is working efficiently. Woking has recently given consent for a number of speculative office refurbishments, which follows on from a very successful programme of town centre regeneration.
 - **East Hampshire** is not currently an established office market, with the majority of demand from local SMEs. However the Whitehill and Bordon Enterprise Zone provides an opportunity to build a more established office based economy, which over time could help

to achieve a critical mass of businesses and provide an attractive location for new investment and business growth.

- **New Forest** is not an established office market and has therefore seen limited demand and limited new supply. In this highly rural district, the priority is to ensure that the local businesses have access to the types of flexible floor space sought after by SMEs.
- ix. These quite diverse challenges mean the impact of permitted development rights (PDR), which allows the conversion of office stock in to residential development, varies considerably across different market areas. To date it has been broadly beneficial (depending on the specific details and location of the development) by removing poor quality stock from the market and providing a much needed source of housing. This is particularly the case in Basingstoke and Andover and Blackwater Valley. However, in all areas there is a concern about the proliferation of residential development in previously commercial areas, which is starkest in Guildford and Winchester town centres. The introduction of PDR means that local authorities no longer have the tools or the power that they need to manage the balance of homes and offices in line with local circumstances. There is therefore a role for the LEP to lobby for reforms to the policy which provide more flexibility and control.
- x. Table 1 provides a summary of the challenges being experienced by market area and the types of intervention which could address these challenges. Given limited resources, we believe the LEP should prioritise those projects where there is evidence that intervention could help to address market failure. We believe the strongest case for LEP support are the following cases:
- **Addressing site constraints:** where sites are in high demand areas but face particular constraints, either because of the costs of remediation on brownfield sites or complicated town centre schemes involving several landowners. An example would be Station Approach in Winchester.
 - **Shared workspace for digital start-ups:** where there are specialist non-standard property needs (eg flexible leases) that are not routinely delivered by the market and also where there are spillover/clustering benefits from similar firms being co-located in their start-up and early growth phases. Any investments should be subject to evidence of unmet demand. The refurbishment of existing space in Basing View is one potential example, although there may be opportunities in a number of locations which have large clusters of digital businesses (including Guildford, Woking and Upper M3).
- xi. There are other examples where there may be a case for intervention, although these will require more detailed consideration by the LEP. This relates to established office markets which currently attract low rental values, where investors are reluctant to invest in new schemes due to fears about a viability gap (this includes Basingstoke and certain towns within Blackwater Valley). In these circumstances, LEP investment could be used to pump prime development, however this should be carefully weighed against trends in the office market. The low rental values may reflect the stage of the business cycle, and wider measures to reduce the oversupply of poor quality space could be effective in attracting private investment over time. This is not to say that these investments should not be supported. They can often act as the signal that the market needs for further investment. However there is a danger that the main effect of public investment may just be the delivery of new office floorspace at an earlier date than would have otherwise been the case.

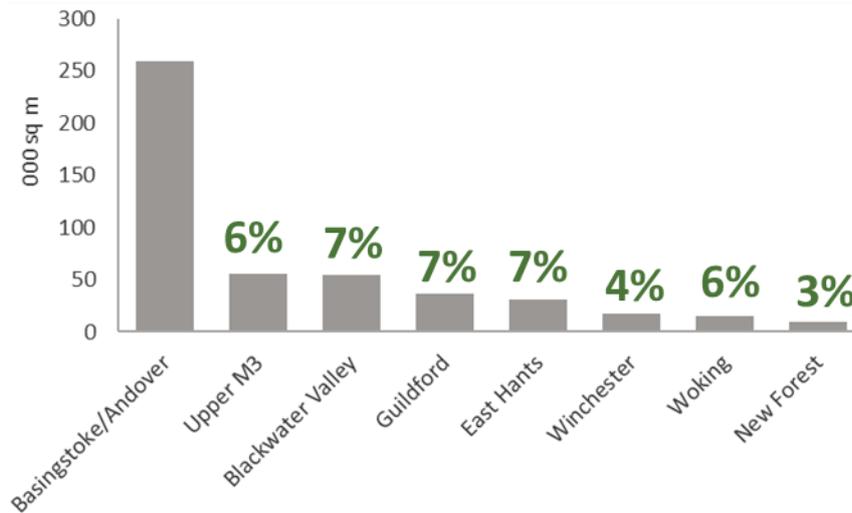
Table 1 Summary of Challenges by Market Area

Type	Examples	Challenges	Case for Intervention
Current High Demand	<ul style="list-style-type: none"> • Upper M3 • Guildford • Woking • Winchester 	Market working efficiently But shortage of sites in some locations (Guildford & Winchester town centres)	<ul style="list-style-type: none"> • Public intervention required to unlock sites where constraints make development unviable • Market failure arguments: co-ordination failures, negative externalities • Example Projects: transport investments, sites in multiple ownerships, site remediation, sector specific workspace
Challenged Office Markets	<ul style="list-style-type: none"> • Blackwater Valley • Basingstoke & Andover 	Established office markets but oversupply of low quality space – not meeting occupier requirements New development unlikely due to low rental values	<ul style="list-style-type: none"> • Public intervention required to stimulate and de-risk private investment • Enhanced promotion of specific locations and potential incentive for relocation • Market failure arguments: lock-in failures, negative externalities • Example Projects: investment in publicly owned offices, demolition/conversion to other uses, sector specific workspace
Potential growth locations	<ul style="list-style-type: none"> • East Hampshire 	Not an established office market but opportunity to develop office market alongside significant investment	<ul style="list-style-type: none"> • Need for bold and ambitious marketing to secure investment in new sites • Investment in new office space targeted at SMEs to develop reputation as office location
Lower current Demand	<ul style="list-style-type: none"> • New Forest 	Market working efficiently But very low demand for office space	<ul style="list-style-type: none"> • No market failure case for public intervention – demand is just low • Social equity case for some investments to avoid deterioration of the local economy • Example Projects: managed workspace for local SMEs

Industrial Market

- xii. The study has found a very different pattern of demand and supply in the industrial market, which includes both manufacturing and warehousing space. There remains a persistent shortage of both industrial space and land with development potential in most market areas, making this by the far the most pressing cross-LEP priority. Even in Basingstoke and Andover, where there is a very large supply of vacant space at Andover Business Park, agents reported shortages of smaller scale industrial space on the edge of Basingstoke.
- xiii. The undersupply of industrial space (particularly B8) transcends LEP boundaries, with very strong demand for any sites that can serve the London market. In the south of the LEP area, the undersupply of sites to serve the Southampton market is shared with the Solent LEP.

Vacant Industrial Space, December 2015



Source EGi. Approximate vacancy rates are shown in green. The percentage is not shown for Basingstoke and Andover due to uncertainty about the total stock of space

- xiv. Local planning authorities face a number of constraints in identifying new sites for industrial development. This includes environmental constraints such as the Green Belt, the lack of political will to identify new sites for uses which generate few jobs, are land hungry and unpopular among local people, and finally face intense competition for much higher value uses, including residential development. This is exemplified by the recent loss of Hartland Park for residential development, which means there are no large sites suitable for large scale warehousing remaining in the north east of the LEP.
- xv. Councils also have few incentives to increase the supply of B8 space because the adverse consequences of undersupply may be shared across a wide area and may have limited direct impact on the local economy. The methodologies used to quantify the need for B8 in employment land reviews rarely have any mechanism for addressing these regional shortfalls.
- xvi. There therefore needs to be some planning mechanism for ensuring that local authorities take collective action, such as a strategic planning statement. A possible model for this is the Heathrow Strategic Planning Group which will be looking at demand for employment floorspace (including B8) around the airport, and will include the Upper M3 and some other local authorities.
- xvii. The role of the LEP should be to:
 - Work with neighbouring LEPs to build a clear picture of the undersupply of sites and undertake research to understand how this is damaging local economies. This should look at the potential impact on consumers but also the productivity impacts on important sectors such as retail and manufacturing where employers are increasingly reliant on just in time deliveries.
 - Recognise the shortage of industrial sites as a cross LEP priority in the next draft of the SEP, and use the evidence in this report and any cross-LEP work to make the case to local authorities as they prepare their local plans and updates.

Other LEP Actions

- xviii. The research has also identified a number of other possible actions that the LEP could take to support the development of the commercial property market:
- **Action 1: Ensuring the LEP acts as a conduit for information sharing.** Decision making for land and property interventions needs to be based on robust and up to date evidence. Some LPAs have limited information on the characteristics of their local businesses or trends in the demand of commercial floor space. There is a need for a consistent set of indicators that all councils could use to monitor development trends in their area, and can be shared with the LEP on an annual basis. The LEP should then provide LPAs with information on local business trends and characteristics by subscribing to business and commercial databases.
 - **Action 2: Improved inward investment monitoring:** At the moment, there is inconsistency in the way that Invest in Hampshire and Invest in Surrey collect information on inward investment enquiries and share this with the LEP (although UK Trade and Investment (UKTI) do monitor and share information on inward investment successes). Better information collection and sharing would mean that the LEP have detailed intelligence on the nature of demand from investors and could work with local authorities to ensure that this demand is satisfied.
 - **Action 3: Improved inward investment positioning and marketing.** Following on from the above, the LEP should work with both Invest in Hampshire and Invest in Surrey to ensure that both, along with the LEP, are focused on the opportunities from London relocations in the next few years and that their strategies are aligned as far as possible. Where there are shared sectors e.g. digital/gaming and cyber securities Invest in Hampshire and Invest in Surrey should develop joint sector propositions. Through these propositions the LEP should also look to develop stronger links with commercial partners (agents etc) who can help to generate leads and drive the capture of new FDI in the Enterprise M3 LEP area. The LEP should also provide strategic support in developing the marketing and inward investment offer of the Enterprise Zones and core town centre locations.
 - **Action 4: Reviewing the impact of PDR and lobbying if necessary.** Although the impact of PDR has been broadly positive to date, there is growing evidence that it is having a damaging impact on the sustainability of a number of local market areas. The LEP needs to be in a well-informed position to comment on the impact of PDR as it is kept under review by the Government. Key to this is good evidence on the nature of the office stock which is being lost and whether it is occupied. This will provide the LEP with an evidence base that it can review and use to lobby Government if necessary.
 - **Action 5: Support improved public sector asset strategy.** Enterprise M3 should look to provide expertise to local authorities on the use of their assets, particularly where they own significant assets which could be used to support economic growth.