

ROTHERHAM BOROUGH COUNCIL – REPORT TO MEMBERS

1.	Meeting:	Cabinet
2.	Date:	6th November 2013
3.	Title:	Investing to Stimulate Further Development at the Advanced Manufacturing Park
4.	Directorate:	Environment & Development Services

5. Summary

The Advanced Manufacturing Park (AMP) continues to attract interest from businesses looking to invest. However, in the current financial climate financing speculative development, even at a premier location such as the AMP, through conventional means is not achievable. This is acting as a barrier to development and growth with some businesses being unable to find suitable property at the AMP that meets their needs.

Working with the landowner and the European Union funded JESSICA (Joint European Support for Sustainable Investment in City Areas) programme the Council can unlock development by forward funding a development scheme. This will enable businesses to create jobs and wealth in Rotherham and generate additional business rates.

The proposal is a direct match to Priority 1 of the draft Rotherham Council Corporate Plan 2013-16, “We will market Rotherham as an attractive business location by investing in initiatives to promote business growth”

The Independent Economic Review identifies that Sheffield City Region has a “private sector job deficit” of about 65,000 compared to the national average; which is spread across a wide range of sectors. Around half of these “missing” jobs are in higher skilled occupations. Unlocking development at the AMP is a significant intervention that the council can make to attract high value jobs.

6. Recommendations

- i) **The Council agrees to forward fund development at the AMP on terms to be agreed by the Strategic Director, Environment and Development Services in consultation with Cabinet Member for Regeneration and Development subject to: -**
 - a) **Confirmation of the detailed costs of purchase and anticipated revenues.**

- b) That the purchase is predicated on the council holding the asset for up to a maximum of 5 years and that the full overall cost and revenue shows a positive outcome.
- ii) That the Strategic Director, Environment and Development Services enters into negotiations with the Local Enterprise Partnership to secure funding to further enhance the viability of the proposal.

7. Proposals and Details

The Advanced Manufacturing Park (AMP) is the UK's premier advanced manufacturing technology park. Businesses located on the park provide world-class advanced manufacturing technology solutions centred on materials and structures typically used in precision industries including; aerospace, automotive, medical devices, sport, environmental and energy, oil and gas, defence and construction.

The AMP is home to world-class research and manufacturing organisations, such as; the University of Sheffield's AMRC with Boeing; Rolls Royce; Castings Technology International (Cti); Dormer Tools, Sandvik Coromant, TWI's Yorkshire Technology Centre and the new Nuclear AMRC.

The site has been developed over the last 10 years to include small office, workshop and lab space, medium-sized hybrid and light industrial units and larger custom-built research, training and manufacturing facilities. The early phases of development have been successful and all buildings on the site are full; the only property offer currently available for new investors is a land purchase or design and build. The AMP site is in the ownership of Harworth Estates which is a property company that grew out of UK Coal. Formal separation from the mining company was achieved in December 2012.

Further successful development of the AMP is a key component in delivering future economic growth in Rotherham and the city region. The success of the AMP is deemed critical to the growth of the Sheffield City Region's economy by the Sheffield City Region Local Enterprise Partnership (LEP) and other public sector partners (including local authorities and the Homes and Communities Agency).

Evolution was a development phase which focussed on providing speculative build and has been highly successful in attracting a range of advanced engineering businesses including university spin outs such as Xeros, precision engineering companies like IIDEA and X-cel, research and development projects such as those undertaken on site by Rolls-Royce, technical and sales offices e.g. Liebherr and international manufacturers such as Dormer, and Sandvik

Harworth now wish to develop an additional phase to attract a range of potential occupiers and have branded this phase R-evolution. R-evolution will comprise around 100,000 sq ft of high quality space targeted at (but not exclusively for) the type of businesses that make up the Rolls-Royce supply chain.

Delivery Options

Harworth would like to be able to develop the space speculatively i.e. without firm commitment from potential occupiers. However, delivery of R-evolution presents a number of commercial challenges.

Harworth has a good level of interest in the space. Independent market advice shows that the availability of equivalent quality stock is reducing, and that at current rates of take up, there is just over 12 mths of supply in the market with no new schemes planned. **Despite these favourable conditions, in the current financial climate of tightened access to finance and bank reluctance to lend against property, financing speculative development with senior debt from banks is simply not possible.**

Equity providers similarly would not provide funding for speculative development unless a very strong return on that equity is guaranteed. This is a commitment that Harworth (or any other developer) is unable to give at present due to the underlying market conditions.

Harworth Estates have similarly had some financial difficulties with the insolvency of UK Coal and the general high level of indebtedness within the group. Therefore Harworth's ability to access finance for development or to put any further capital at risk is significantly diminished.

This is a classic case of market failure; there is demand from advanced manufacturing companies to locate on the AMP and to the opportunity to make space available, facilitating a next phase of growth which will attract and secure quality jobs and wealth in Rotherham. However, this is not deliverable through conventional means in the current economic climate.

The Proposed Delivery Option

In order to address the above challenges the Council has been working with partners within the City Region to explore how the development could be brought forward. In October 2012 the City Region constituted a JESSICA (Joint European Support for Sustainable Investment in City Areas) fund for which Sheffield City Council are the accountable body. Through an OJEU (Official Journal of the European Union) procurement process property consultancy CBRE were appointed fund manager in December 2012.

The SCR JESSICA fund is a public fund of around £23M which comprises £15M European Regional Development Fund match with £8M Growing Places Fund from the SCR LEP.

The fund is a revolving fund which has the purpose of helping to facilitate and drive economic growth through investment in physical infrastructure.

It is likely therefore that the SCR JESSICA will be able to provide the development finance for the project and the detailed due diligence process for this is underway between Harworth Estates and the fund manager CBRE. However, the fund is only

intended to provide finance for the development phase of a project in order that funds can be recycled and re-invested into other projects. There therefore needs to be provision for the loan to be repaid within a defined timescale.

This would typically be either through a market sale of the completed development to a third party or through the refinancing of the loan with an alternative financier. As indicated earlier, in the current scenario, refinancing with an alternative financier would be very unlikely and achieving a market sale would be contingent upon the lettings achieved and the strength of the rental income stream provided by any occupiers. This is clearly an uncertain position and hence makes the market exit uncertain.

Without a certain exit the SCR JESSICA fund would be unable to provide the development finance and the project would not happen.

It is proposed the Council unlock development by providing the exit i.e. agreeing the purchase of the development on completion of construction in return for receiving the revenue generated from rent. It is therefore proposed that RMBC purchase the completed development thereby having the following impact:

- Enables the development to come forward.
- Provides the exit to enable repayment of the SCR JESSICA loan to allow reinvestment in another project
- Secures investment in Rotherham and in the Sheffield City Region
- Secures and facilitates jobs in Rotherham – based on Homes and Communities Agency standard employment densities for a light industrial building on a business park of 47m² per job this scheme would provide 102 jobs.
- Provides a income stream to offset borrowing costs to facilitate the purchase
- Generates an increase in business rates. Based on existing assessments and the current multiplier this is likely to be in excess of £100,000 per annum. As this scheme is in the Enterprise Zone the growth in business rates would be retained by the LEP.

8. Finance

A key condition to be fulfilled for the purchase to proceed is that the scheme is cost neutral or generates an overall surplus to the Council on realisation of the asset. The purchase will only proceed on this basis.

RMBC are in a unique position to facilitate this development due to their ability to access capital at low levels of interest from the Public Works Loan Board

The Director of Finance will advise on funding alternatives and source appropriate finance to minimise the cost and exposure to the Council of borrowing to fund the purchase.

The cost of prudential borrowing and any other associated revenue costs will be carried by Environment and Development Services. This cost will be met by the

income generated from the development. The intention is that annual revenue income covers both the capital financing costs and all other associated revenue expenditure on a year by year basis. This will be a key factor in the Strategic Director for Environment and Development Services and Cabinet Member for Regeneration and Development agreeing terms for the Council to proceed with the purchase.

9. Risks and Uncertainties

This proposal is that RMBC will hold and manage the investment on the basis that the projected gross (and net) rental income will cover the costs of borrowing and potentially return some excess to support the revenue account.

The risks associated are as follows:

- Harworth Estates fail to construct the development
- Some or all of the units fail to let
- Some or all of the units fail to let on suitable terms
- The rental achieved fails to reach the expected rental per square foot per annum
- Any occupier becomes insolvent

Risk will be managed and mitigated through the following:-

- The council will purchase the development on practical completion. Until the building is completed and handed over as agreed the Council will not hand over the purchase price.
- The estimated construction cost has been reviewed by the Director of Asset Management and is considered reasonable. Construction will be procured by Harworth Estates through a tender exercise with the Council having the ability to review the actual construction cost and other costs prior to proceeding with the purchase.
- Structuring the deal such that the price for the completed investment varies according to the lettings secured prior to the Council completing the purchase i.e. the purchase price is reduced if the development is not let to an occupier prior to practical completion of construction. This will ensure that Harworth are incentivised to continue to promote the scheme and secure suitable lettings.
- Negotiating a “non-competition clause” preventing Harworth from building competing units of a similar size until the first phase is let and including an agreement as part of the purchase agreement that all enquires to take space on the park are directed toward these units.
- In addition to the marketing done by Harworth, Rotherham Investment and Development Office will continue to market the site to potential investors. Independent market advice indicates that there is only 12 months of supply of similar quality space available (based on current take up rates) and no competing speculative developments in the pipeline. The advice also indicates that lettings in this prime location are very achievable at rents that would make the proposal viable with minimal tenant incentives. There is evidence of interest from potential occupiers at rentals above this base level which if

achieved will enhance the viability of the proposal and gives the confidence that should any unit become vacant there is strong demand to facilitate re-letting.

- The investment going into the AMP from occupiers such as Rolls-Royce and the AMRC is likely to enhance the site and values over time. This will be prime real estate on an internationally significant manufacturing park.
- Units will be let on a full repairing and insuring basis with the occupier responsible for payment of a service charge for common services meaning that once let the council's management and administration costs are the only deduction from gross rent to net rent.
- Submission of applications to secure grant funding to reduce the exposure. Discussions have been initiated on using unallocated Growing Places Fund monies for this purpose, other alternatives will be pursued as they arise.
- Initiating discussions with city-region partners to explore whether some of the increased business rates retained by the LEP should be returned to the Council thereby increasing gross revenue.

10. Policy and Performance Agenda Implications

The proposal is a direct match to Priority 1 of the draft Rotherham Council Corporate Plan 2013-16, "We will market Rotherham as an attractive business location by investing in initiatives to promote business growth"

The Independent Economic Review identifies that Sheffield City Region has a "private sector job deficit" of about 65,000 compared to the national average; which is spread across a wide range of sectors. Around half of these "missing" jobs are in higher skilled occupations. Unlocking development at the AMP is a significant intervention that the council can make to attract high value jobs.

The project has direct impact on delivering the objectives of the growth plan: -

- "We will ensure we get the land offer right and that we are responsive to investors' needs, even where this may not fully align with our own plans. We will identify how property could be developed for investors seeking premises for immediate occupation".
- "We will develop a better understanding of the challenges SCR firms face in accessing finance. We will then explore how new and innovative investment mechanisms could be used to address these challenges".
- "We will bring forward key development sites in the right locations"

The proposal facilitates the deployment of JESSICA funding making a major contribution towards meeting ERDF business plan targets, maintaining the integrity of the JESSICA fund and keeping the available funding within the City Region. The potential timescales for the AMP project will allow the JESSICA loan to be repaid in 2014 making money available for 2nd round investments. Further recycling the JESSICA fund allows additional investments to be made in other use classes such

as retail and residential development and provides an opportunity to address many of the town centre priorities in Rotherham and the City Region.

11. Background Papers and Consultation

SLT, 4th November 2013

CSART, 30 September 2013

Contact Names:

Tim O'Connell, RiDO

Ext: 54563; e-mail: tim.oconnell@rotherham.gov.uk