



Report To: Performance & Investment Committee
Subject: Glasshouse investment business case (Alderley Park)
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1. Purpose

This paper presents a proposal to make a £3.87m investment to Alderley Park Limited (APL) in the Glasshouse scheme (Block 15) to create 148,000 sq ft of new speculative Grade B+ office floorspace at Alderley Park. The Glasshouse scheme could generate c.£792k per annum in retained business rates, providing a payback period of 4.8 years and potentially generating up to £17.4m in retained business rates over the remaining lifetime of the Enterprise Zone.

2. Recommendation

That the Performance & Investment Committee ratifies the decision of the Enterprise Zone Board to approve the investment of £3.87m in the Glasshouse (Block 15) at Alderley Park.

3. Background

APL is seeking £3.87m of EZ investment to deliver a £13.99m project (Phase 2) to redevelop Block 15, known as the Glasshouse at Alderley Park, which will provide 148,000 sq ft (13,784 sqm) of Grade B+ commercial office space. APL is seeking EZ funding because there is a gap in the project's financial viability which means that it does not meet their minimum internal rate of return (IRR) of 15%. £14.1m has already been invested by APL in the project through the Phase 1 works, bringing the total project cost up to £26.95m. The full Glasshouse business case is attached as **Appendix A**.

Cushman & Wakefield's technical appraisal of the proposed investment (**Appendix B**) concludes that overall the project "*may be considered a fundable scheme under the aspirations established within the overarching EZ Investment Strategy*", noting the following:

- The project provides a clear strategic fit with the vision and objectives set out in the EZ's Development and Investment Strategy, particularly in terms of maximising the benefits of business rate discounts within the first 5-years, attracting science-based companies and creating high value jobs in target sectors.
- The project provides a clear case for public intervention. AstraZeneca's slower than anticipated rate of decantation has left Alderley Park with a lack of supply of commercial office space ready and available for occupation. As a result, APL have been forced to bring forward more complex schemes such as the Glasshouse. The high costs of repurposing

Block 15 which was formerly in-vivo lab space relative to achievable office rental values presents a financially unviable position relative to APL's required rate of return (IRR). As such without public intervention, APL would not pursue the project further.

- The project provides good value for money in terms of number and cost of jobs created, economic impact and private sector leverage and in terms of the likely level of retained business rates generated over the lifetime of the EZ, which the LEP will be able to reinvest in other economic development projects.
- The anticipated benefits are in line with what they would expect of a project of this scale and nature, although APL appear to have overestimated the likely GVA per job and retained business rates estimates.
- APL's revised estimates of rateable value of £1.69m would produce retained business rates of c.£828k per annum (based on current ratings multipliers and assuming full occupation) provides a more robust estimate of likely business rate income from the Glasshouse, although Cushman & Wakefield advise that the VOA would be likely to round down the RV to £1,65m, which would produce c.£792k in retained business rates per annum. On this basis the £3.87m EZ investment would payback in 4.8 years.
- The project can make a strong case for supporting the aspirations of the EZ, particularly in the critical short term whilst Business Rate Discount incentives are available, in terms of delivering new employment floorspace, attracting science sector businesses and creating high value jobs in target sectors. It also has potential to generate a significant 'return on investment' for the EZ over the remaining 22 years of the programme which could be re-invested into future projects.

4. Term sheet

An Investment Agreement has been drawn up by Weightmans (acting for the LEP) and Addleshaw Goddard (acting for APL). The Investment Agreement is based on commonly used precedents from other LEP/public sector investments. The term sheet setting out the key commercial terms in the legal agreement is attached at **Appendix C**.

5. State Aid

Addleshaw Goddard have provided a State Aid opinion which indicates that they will seek exemption under Article 56 of GEER, which provides an exemption to the State aid rules where the funding is used for investment in local infrastructures. The requirements of Article 56 are as follows:

The funding must be used for the "Financing for the construction or upgrade of local infrastructures which concerns infrastructure that contribute at a local level to improving the business and consumer environment and modernising and developing the industrial base" (Article 56(1)).

Weightmans have reviewed the State Aid opinion provided by Addleshaw Goddard and have concluded that it is sound and thorough and have signed it off.

6. Funding

The proposal is to effectively provide 'gap funding' to APL to bridge the viability gap in the project. Gap funding is a tried and tested method of underwriting speculative development and our property advisers Cushman & Wakefield have provided examples of a number of other LEP's currently providing 'gap funding' including:

- Liverpool Combined Authority utilising their Single Investment Fund (SIF) to support the development of a 105,000 sq ft speculative industrial unit to plug a viability gap
- South East Midlands Local Enterprise Partnership has provided £1.2m of gap funding for a speculative commercial scheme
- EM3 LEP provided gap funding for Basingstoke and Deane Council to deliver a new build innovation centre.

The proposal is to utilise the LEP's Growing Places Fund (GPF) to fund the Glasshouse investment. GPF is a loan fund and the LEP would repay the GPF investment through the retained business rates from the Glasshouse with interest at 1% above Public Loans Works Board base rate.

7. Benefits

APL estimate that the project will deliver the following benefits:

- 13,784 sqm (148,375 sq ft) of commercial office space
- 25-50 new businesses accommodated
- Business rate retention/uplift of c.£828k per annum
- 1,200 tenant jobs created
- 224 temporary construction jobs supported
- £120 million GVA per annum
- £15 million additional private sector investment

Overall Cushman & Wakefield report that the anticipated benefits are in line with what they would expect of a project of this scale and nature. However, they note that APL appear to have overestimated the likely Gross Value Added (GVA) benefits. They note that GVA has been estimated at £120m per annum, which equates to £100,000 per tenant job, which is significantly higher than the C&WLEP average productivity figure estimate of £34,000 per job per annum in the sub region. Nevertheless, the GVA at Alderley is likely to be significantly higher than the C&WLEP sub-region average given the highly skilled nature of the jobs created in the biotech sector.

As noted above, APL's revised retained business rates estimates of c.£828k per annum, provides a more robust estimate of likely business rate income from the Glasshouse than their original figure of £1,2m. However, Cushman & Wakefield suggest that the VOA would be likely to round down the RV to £1,650,000, which produce c.£792k in retained business rates per annum. On this basis the £3.87m EZ investment would payback between 4.6 to 5 years, depending on occupancy rates.

8. Risks

There are five key risks for the LEP associated with this investment:

- a) **Business rate income** – The level of retained business rates generated is a key driver for the LEP and EZ Board in any investment as it effectively represents our return on investment (ROI) and enables the LEP and EZ Board to invest in future economic development projects both within the EZ and wider Cheshire Science Corridor. As such realistic estimates of business rate income are important when considering EZ investments. As notes earlier in this paper, APL has provided a more detailed ratings valuation for the Glasshouse, which estimates a Rateable Value (RV) of £1.69m. Based on current ratings multipliers this would produce estimated annual business rates of £828k assuming full occupation. In the first year, the level of business rates payable could be as low as £621k (assuming no occupancy) taking account of the 3-month void rate relief on offices. The estimated ratings valuation provided by APL is based on an average of £123 per sqm (£11.40 per sq ft). This is a relatively conservative estimate in comparison with the current average RV across Alderley Park of £133 per sqm. As such, the more detailed ratings valuation produced by APL provides a more robust estimate of likely business rate income from the Glasshouse. Cushman & Wakefield have reviewed APL's revised business rate estimates and have agreed that the unit rates applied are reasonable. However, they have applied a more realistic 'rounding' approach as would be taken by the VOA to round down the estimated RV's per level and per block – see attached excel document. This brings the total RV down slightly from £1,690,000 to £1,650,000. On this basis the £3.87m EZ investment would payback within 4.8 years.
- b) **Delivery** – a key risk is associated with the ability of APL to deliver the proposed development on time and to budget. This risk is significantly mitigated by the track record of the Alderley Park team and in particular Bruntwood, APL's major shareholder, which is a large developer with an extensive track record of delivering high value and complex redevelopment projects of this nature.
- c) **Occupation** – this is a speculative office development, without any pre-lets in place. As such, a key risk is lack of take-up of the new space by occupiers. However, APL report that office occupiers are currently being turned away or directed to unsuitable space due to the lack of existing supply at Alderley Park and have provided a schedule of recent office deals and enquiries which indicates that a total over 100,000 sq ft of office space is currently under negotiation and a further 90,000 sq ft at active enquiry stage. Cushman & Wakefield advise that demand is strong in the North Cheshire office market and that good quality available stock is in short supply.
- d) **Rate mitigation** – a key risk for the EZ Board is the deployment of rate mitigation strategies by the landlord, which could see retained business rates reduced by up to 75% if the premises are not occupied by tenants. However, APL have committed not to deploy any rate mitigation strategies in relation to the Glasshouse and this has been built into the Investment Agreement. This means that the LEP will receive 100% of the retained business

rates after the initial 3-month 'void rates' holiday, regardless of whether the premises are occupied.

- e) **State Aid** – we have to ensure that any public investment is State Aid compliant. Our legal advisers Weightmans have signed off the State Aid opinion provided by APL's legal advisers, Addleshaw Goddard. In the event that the investment is deemed not to be State Aid compliant, APL would be required to repay the full amount of the LEP's investment.

9. Conclusions and recommendations

Overall the Glasshouse proposal represents a good investment for the Enterprise Zone. It fits with the vision, strategic objectives and investment priorities set out in the EZ Development and Investment Strategy and could provide a good ROI in terms of retained business rates and wider economic benefits to the Cheshire Science Corridor and sub-region.

It is, therefore, recommended that the Performance & Investment ratifies decision of the EZ Board to make an investment of £3.87m in the Glasshouse (Block 15) at Alderley Park as set out in the key commercial terms set out at Appendix C of this report.