

Report of:	Executive Member for Regeneration Executive Member for Environment, Finance and Governance Director of Regeneration and Culture Director of Finance
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Submitted to:	Executive
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Date:	10 May 2022
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Title:	Tees Advanced Manufacturing Park - Next Phase - PART A
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Report for:	Decision
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Status:	Public
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Strategic priority:	Town centre
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Key decision:	Yes
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Why:	Decision(s) will incur expenditure or savings above £150,000
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Urgent:	No
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Why:	Not applicable
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Executive summary

This report proposes the development of a second phase at Tees Advanced Manufacturing Park (TeesAMP), funded by Middlesbrough Council (£8.82m), subject to complementary funding from Tees Valley Combined Authority (TVCA); and, an additional £335k to balance the first phase development budget.

The following is asked of the Executive:

- a) that the information contained in Part A of the report be noted; and
- b) that the decision be taken once all the financial or exempt information contained in Part B of the report has been considered.

Other options have been appraised by external consultants, including doing nothing, asset disposals and the Council assuming all development risk. The proposed Council and TVCA funded second phase will ensure a high quality development, with maximum risk mitigation and benefits realisation.

The principal implication of the proposal is an increase in prudential borrowing; the costs of which are projected to be more than offset by income generation over the term.

Purpose

1. This report proposes the development of a second phase at TeesAMP, funded by Middlesbrough Council (£8.82m), subject to complementary funding from Tees Valley Combined Authority; and, an additional £335k to balance the first phase development budget.

Background and relevant information

2. On 19th December 2017, the Executive approved two reports titled *Tees Advanced Manufacturing Park – Delivery and Investment Enablement [Parts A and B]*, which enabled a first phase development of 180,000 sq. ft. of Council-owned light-industrial units. The Council subsequently appointed Cleveland Property Investments Ltd. (CPIL) as developer, with the construction contract completed by Robertson North East England in June 2020; the scale of the resultant development being slightly ahead of target at 181,764 sq. ft. (see Appendix 1).
3. The Executive approval on 19th December 2017 also included the market rate sale of:
 - a. a single plot adjacent to the existing TWI facility to support its expansion ambitions; and
 - b. two plots to CPIL at the northerly and southerly extremities of the site, for an Anaerobic Digester (AD) and a Gas Plant respectively.

TeesAMP Phase 1

First Phase Development Budget

4. The £22.46m first phase development was funded by Middlesbrough Council (£12.523m), Tees Valley Combined Authority (£7.65m) and SSI Task Force (£2.3m).

Lettings Income & Expenditure

5. Despite the economic impact of the global pandemic, the first phase is now 100% let to tenants including Firth Vickers-Paralloy, Cupral, Sultzer, Durata, Ace Aluminium and Flexitallic.
6. The first phase has exceeded expectations markedly, with annual rental income significantly above forecasts (see Part B of this report for further details) and the average lease achieving a term certain of seven years. The higher rents have resulted in proportionately higher developer incentive and commercial agents' fees. Coupled with variations to upgrade power supplies and additional security measures; it is proposed that £335k is approved in order to balance the first phase budget.

Award

7. In acknowledgement of its success, TeesAMP was named Commercial Development of the Year at the Insider North East Property Awards 2021.

Plot Sales

8. The intended plot sale of 1.959 acres to TWI completed on 16th November 2020 realising a capital receipt of £216,943. On this plot TWI is to construct an additional

12,500 sq. ft. Materials Testing Facility; and Teesside University will complete the construction of the £13.1m Net Zero Industry Innovation Centre (Appendix 2) in 2023.

9. Due to planning restrictions on the developable area of the Gas Plant site, accompanied by a new inward investment opportunity; on 14th July 2020, an Executive decision approved the sale of an alternative 3 acre site in replacement for the original Gas Plant site, with a deadline to complete the sale by 14th December 2020, aligned to the sale of the AD site.
10. Despite considerable endeavours, CPIL was unable to successfully conclude negotiations with the inward investors in respect of both sites; with the options lapsing following two national lockdowns on 14th December 2020.
11. On 23rd March 2021, a further Executive decision approved a new conditional site development option in favour of CPIL which included the sale of the AD site (3.5 acres) for £400,000, with the sale completing on 22nd November 2021.
12. The Council has therefore realised plot sale capital receipts totalling £616,943. The valuations agreed for the plots at TeesAMP were c. £114,000 per acre at the time of sale. Land prices elsewhere at Riverside Park are generally significantly lower. At the time of writing (1st February 2022), Connect Property North East Ltd was marketing a 5.7 acre site for £385,000 – equivalent to £67,544 per acre¹.

Second Phase Land

Cushman & Wakefield Debenham Tie Leung – Update Report – TeesAMP

13. In March 2022, Cushman & Wakefield Debenham Tie Leung (C+W) completed a two part review on the first phase development value and demand within the light-industrial sector moving forward.

Land Disposal Value

14. The report noted that two substantial and contractually unencumbered plots of land remain within the Council's ownership for development or disposal; measuring 3.9 acres and 3.7 acres (see Appendix 3, shown as red and green boundaries respectively). C+W has advised that²:
 - a. notionally, the disposal of the 7.6 acres second phase provides a "site value of £2.00m *before* deduction of abnormals"; and
 - b. development of further units on the 7.6 acres would realise a significant land value uplift.
15. Summary development disposal valuations are set out in Part B of this report.
16. Overall, the report concluded that the Council's original £12.523m investment in the first phase has realised a significant uplift in asset values, and is simultaneously providing considerable revenue income. This has stimulated investment in Middlesbrough, uplifted land values and has incentivised investment in nearby land and property assets.

¹ CoStar Group, Inc., 2022. Realla, Commercial land for sale, Middlesbrough. [Online]. [Accessed 1 February 2022]. Available from: <https://www.realla.co.uk/details/10940601>

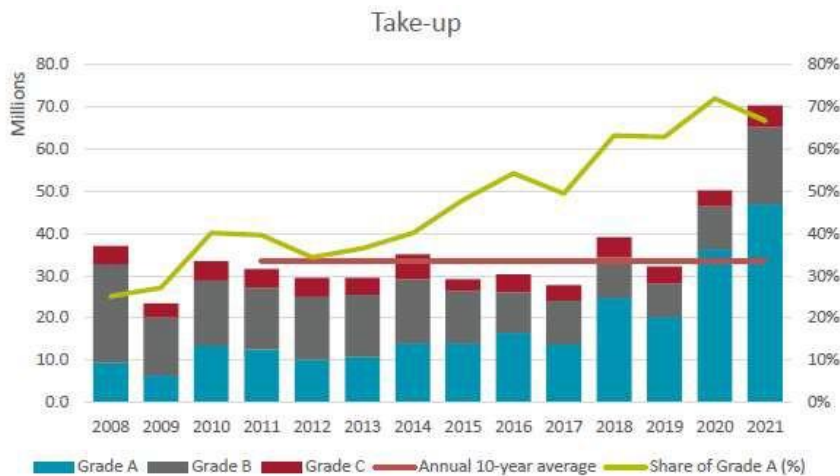
² Cushman & Wakefield Debenham Tie Leung, 2022. Update Report – TeesAMP Middlesbrough.

17. Further development therefore provides an opportunity to secure additional capital receipts, or, substantially increased asset valuations coupled with additional annual rental income to support the Council's financial position more generally.

Sectoral Demand 2

18. The UK logistics and industrial market reached new heights in 2021. Take-up soared to an all-time high of 70.1 million sq. ft., some 32% more than the previous record of 53 million sq. ft. in 2020 and more than double the amount of space transacted during a pre-pandemic year.

19. Occupier demand for space has focused on good quality floor space, particularly newly built Grade A. Over 40 million sq. ft. of new space was taken by occupiers in 2021 and for the first time on record, more speculative space (20.6 million sq. ft.) was taken than built-to-suit.



20. In response to this exceptional occupier demand, developers have delivered almost double the volume of speculative space as in 2020: 13.7 million sq. ft. was completed in 2021, up from 7.3 million sq. ft. in 2020. The development pipeline for 2022 is even bigger, with over 15 million sq. ft. of space currently under construction.

21. The strength of occupier demand has translated into faster letting periods for speculative schemes: 75% of the units completed in 2020-2021 have let already. Despite this developer activity, logistics and industrial availability in the UK is at its lowest level ever recorded at 44.7 million sq. ft. This represents less than half the 95.0 million sq. ft. available at the market peak in March 2010.



Development Business Case

22. To ascertain the relative benefits versus costs of development, the template first phase business case has been updated to model a notional second phase of up to 90,000 sq. ft. The detailed modelling set out in Part B of this report contains commercially sensitive income and construction cost assumptions. The due diligence completed alongside the C+W Update Report, points to several abnormal risks which would almost certainly negatively impact any land disposal, set out as follows:
- a. *Utilities* – Development of the first phase provided electricity supplies up to three times the standard on industrial developments of similar scale. However, a number of the existing tenants are advanced manufacturers with particularly energy intensive operations, which has denuded the supply earmarked for future phases; resulting in prudent contingencies being required to account for further upgrades.
 - b. *Contamination* – The original site investigations were undertaken by Dunelm and DTA in 2018; and the resultant remediation strategy was completed by Roberts Environmental Ltd. Summary advice prepared by Faithful and Gould noted a particularly high likelihood of significant deep-level contamination (beyond those levels already remediated) being encountered in the 3.9 acre development site. This risk would be initially mitigated through additional localised ground investigations.
 - c. *Heritage* – Victorian-era tunnels of archaeological interest were discovered during construction of the first phase; adjacent to the 3.7 acre development site. Although these discoveries did not ultimately result in development being constrained, it cannot be ruled out that further such discoveries would not incur significant costs or impede development altogether in specific locations. As with the deep-level contamination, this risk would be initially mitigated through additional localised ground investigations.
 - d. *Inflation* – A period of sustained and somewhat uneven construction inflation in the period since C+W completed its Update Report, raises the risk profile for private sector development. This risk would be mitigated by providing a contingency to capture projected inflationary pressures.
23. When the risk factors above are accounted for with sensible contingencies, a traditional Gross Development Value (GDV) appraisal outturns a marginally negative Residual Land Value.
24. Having garnered considerable experience and warranted site-specific information in the development of the first phase, the Council is now better placed than prospective private sector developers to calibrate and mitigate such abnormal development risks. It is highly likely that the abnormal risks highlighted above would remain prohibitive for commercial investors, which would ultimately result in depressed offers for the two sites, were site disposals pursued.

Benefits

25. Commercial investment decisions do not account for measurable economic growth benefits, which in respect of the first phase, includes:
- a. *Employment Growth* – the majority of tenants based within the first phase are still growing operations. Based on current trajectories, is not unreasonable to assume that within 12 to 18 months, between 500 and 1,000 jobs will be based

at TeesAMP, with at least 15% of these being new positions. Assuming a mid-point on jobs, over a five year period, the cumulative Gross Value Added (GVA) impact of these new positions is conservatively estimated to be in excess of £6.7m³. Given the first phase is set to achieve full occupancy, the increasingly positive impact of employment growth will be measured through quarterly monitoring.

- b. *Construction Activity* – 37% of subcontractors employed on the first phase, were based within just 20 miles of the development⁴, creating additional demand within the Tees Valley.

26. In addition to readily measurable benefits, there are several other factors which development will realise, which includes:

- a. linking residents to skilled employment opportunities, making use of transferrable skills from legacy sectors such as steel making;
- b. supporting local supply chains and those who are dependent on local suppliers to generate wealth and employment opportunities;
- c. supporting the local economy through multiplier effects, increasing disposable incomes which, in turn, help support the retail and leisure sectors;
- d. encouraging investment in sectors with high growth potential helps to diversify the local economic mix and increase resilience against economic shocks; and
- e. supporting the retention and growth of existing businesses and the attraction of inward investment.

Regeneration Benefit Cost Ratio (BCR)

27. The Council has utilised the general methodology employed by the Treasury to assess Levelling-Up Fund (LUF) bids, in order to ascertain the relative costs and measurable benefits of an additional c. 90,000 sq. ft. development over a five year period.

28. Whilst the detailed financial metrics and modelling assumption of the BCR are set out in Part B of this report due to commercial sensitivities, the headline outturn of a second phase provides a positive BCR of 3:36.

Break-Even

29. Taking into account the additional abnormal risks and contingencies, the second phase business case demonstrates that break-even would be achieved at c. 70% occupancy, an outturn 5% higher than the break-even point that was calculated for the first phase development.

Objectives of a Second Phase

30. The positive BCR, coupled with the break-even outturn, provides a compelling rationale to proceed with a Council-led development of the two remaining plots. Were the Council to approve a second phase, the headline development objectives would be, in summary:

- a. the completion of TeesAMP as a localised business cluster for advanced manufacturing and its supply chain;

³ Tees Valley Combined Authority, 2019. Tees Valley Economic Assessment. Section 4 - Economic Growth and Productivity (page 24).

⁴ Robertson, 2020. Project Monthly Progress Report – TeesAMP (page 29).

- b. creating between 250 and 500 new jobs and up to 90,000 sq. ft. of high specification, Council-owned light-industrial units;
- c. creating an operational surplus which will cover the costs of development finance and generate a surplus to invest in Council services; and
- d. enhancing the value of existing Council-owned assets.

Securing Complementary Investment

- 31. The development proposal is conditional upon securing the corollary de-risking investment from TVCA as a contribution towards development costs and contingencies. Any TVCA investment would also be subject to the transfer of retained business rates as outlined in Part B.
- 32. The business case set out in Part B of this report has been shared with TVCA and this will be progressed through requisite due diligence. It is anticipated that a report will be presented to TVCA's Cabinet, to consider the proposal and make a formal decision as to whether to support a second phase at TeesAMP.
- 33. TVCA's investment will also be conditional on appropriate safeguards in terms of the development progressing; comfort that the overall scheme is affordable and deliverable; and assurances the financial return is protected for the duration of the collection period.
- 34. It should be noted that these proposals do not result in the Council losing business rates income, as the site is an Enterprise Zone through to 2037, which represents the term of the proposed payback for the funding package. Thereafter, the Council will realise collected business rates income.

Development Management

Procurement and Contractual Arrangements

- 35. It is proposed that the Council's Capital Projects and Design Services teams would develop the design solution through to RIBA Stage 3, inclusive of Strategic Definition, Preparation and Briefing, Concept Design and Spatial Coordination.
- 36. Thereafter, the Council will utilise an existing procurement framework to obtain a Design and Build solution and secure a fixed price for the construction contract. The selection of an appropriate framework would be subject to an internal assessment, dependent, in part, on the fees charged and the quality and standing of contractors available.

Appointments of Specialist Advisors and Commercial Agents

- 37. As part of RIBA Stage 1, the abnormal risks highlighted in this report would be further mitigated through the appointment of specialist advisors to undertake tasks including, but not limited to: ground investigations; utility assessments; archaeological surveys; and highways/traffic surveys. The Council's Capital Projects team would lead on such appointments.
- 38. Following the appointment of a construction contractor, it would also be necessary to appoint commercial letting agents. The most likely arrangement would be the appointment of both a local and national agent, with the standard market rates split

equally between the two, as was the case with the first phase at TeesAMP. The Council's Commercial Finance team would lead on these appointments.

Lease Eligibility Criteria and Incentives

39. The existing TeesAMP Lettings Criteria and Policy would be amended to reflect the revised rents and envisaged incentives within the scope of the second phase business case. Commercial letting agents would be contractually bound to observe these requirements.

Marketing and Communications

40. During the two years since the first phase completed, the Council has internally managed marketing and communications. This has included the production and maintenance of extensive marketing collateral, including the TeesAMP website. Communications campaigns have ensured the significant social media coverage. As part of the business case, an allowance has been made for further marketing costs and it proposed that marketing and communications should remain in-house.

Asset Management and Operations

41. Operationally, TeesAMP is being managed by the Council's Operations and Valuations and Estates services. The same arrangement extends to Boho buildings and the Centre Square office buildings. The estate and facilities management adheres to an institutional standard specification based on fully commercial terms and endorsed by C+W. Tenants are liable for a service charge which recoups maintenance costs associated solely with TeesAMP. It is proposed that the current arrangements be extended to any second phase development.

Milestones

42. As part of RIBA Stage 1, a Project Programme and shall be completed. At this stage, the summary completion milestones are as follows:

a. Business Case and Project Initiation	May 2022
b. Funding Agreement	July 2022
c. RIBA Stages 0-3 Inclusive:	October 2022
i. Site Surveys	
ii. Project Programme	
iii. Project Execution Plan	
iv. Planning Application	
d. Procurement	November 2022
e. Contractor Appointment	January 2023
f. Planning Consent	January 2023
g. Contractor Mobilisation	February 2023
h. Commence Construction	April 2023
i. Sectional Completion (c. 30,000 sq. ft.)	September 2023
j. Practical Completion (c. 90,000 sq. ft.)	February 2024
k. Full Occupation	October 2024

What decision(s) are being recommended?

That the Executive:

- a) that the information contained in Part A of the report be noted; and
- b) that the decision be taken once all the financial or exempt information contained in Part B of the report has been considered.

Rationale for the recommended decision(s)

43. The detailed business case coupled with C+W Update Report conclude that a second phase of development at TeesAMP:
- a. represents a proportionate cost for the development;
 - b. provides a reasonable risk and return profile for the Council; and
 - c. provides the opportunity to realise substantial corollary benefits, as highlighted in paragraphs 25, 26 and 30.

Other potential decision(s) and why these have not been recommended

44. A summary of the options is tabulated as follows

Options	Strategic Fit	Affordability & Value for Money	Conclusion
Do Nothing	<i>No</i> – Lost opportunity and negligent use of a strategic asset.	<i>No</i> – A dormant site will require revenue for maintenance.	Discard
Asset Disposal	<i>No</i> – Risk of lower quality of development and denuded corollary benefit realisation.	<i>No</i> – A sale would generate c. £2m capital receipt, with no future rental income benefit.	Discard
Council funded second phase development	Yes – Ensuring a high quality of development, with corollary benefit realisation	<i>No</i> – The Council would assume all risk mitigation and increase the likely schematic break-even point.	In abeyance
Council and TVCA funded second phase development	Yes – Ensuring a high quality of development, with corollary benefit realisation.	Yes – Reduces risk exposure whilst improving asset value by £3.8m and generating income.	Proceed

Impact(s) of the recommended decision(s)

Legal

45. A funding agreement between Middlesbrough Council and TVCA is required should the latter agree to provide complementary resources. All appointments will be subject either to internal standing orders or procurement frameworks. National standard construction contracts will be utilised.

Strategic priorities and risks

46. The proposal to develop a second phase at TeesAMP directly supports the Strategic Plan as it will both create “iconic new spaces” and “deliver value for money” by securing commercial tenants, growing the Council revenue base.

47. The business case has scoped the abnormal risks, mitigation and associated costs highlighted in paragraph 22. In addition, the business case has accounted for several manageable residual risks including:

- a. *Lettings* – There is an inherent risk of long-term voids with any speculative development. The business case has scoped the potential contingencies for reduced rental and business rates income during the first two years following practical completion. In the unlikely event the second phase struggles to secure appropriate tenancies, it may be necessary to relax the entry criteria to ensure that the site can remain financially viable.
- b. *Local Displacement* – The development of the plots will seek to minimise displacement from the local market. As such, any prospective tenancy which risks significant displacement from within the Tees Valley will have to demonstrate a significant growth or consolidation case in order to access a tenancy on the site. This may include avoiding the prospect of the company seeking an alternative accommodation, outside of the Tees Valley.
- c. *Remediation* – Should the additional site investigations highlight areas of the site which are notionally prohibitive in terms of remediation cost (is beyond the contingencies), the sequential approach shall be:
 - i. *Compacted Foundations* – the presence of contamination may exclude preferred foundations without excessive remediation. Compacted foundations as used in the first phase would require deep excavations but would not require remediation of any material below the excavation. Only excavated material will have to be remediated.
 - ii. *Layout Reconfiguration* – To avoid or encapsulate areas of contamination as per the remediation strategy.
 - iii. *Reduce Development* – In the event that neither compacted foundations or layout reconfiguration mitigate the risk within the available contingency ceiling, the scale of development shall be reduced to meet the business case imperatives.

- d. *Construction Cost* – Should the quoted cost of the works exceeds the target cost of the development, the sequential approach shall be: value engineering; retendering, reduce the scale of development; or, the scheme is aborted (prior to any TVCA resource expenditure).
- e. *Planning* – A second phase of light-industrial units at TeesAMP has existing outline planning consent. Detailed planning consent will be required for a revised layout and increased scale of development, with additional highways/traffic surveys completed to scope the impact.

Human Rights, Equality and Data Protection

48. An Impact Assessment is not required as the proposals will not have an impact on protected groups. In addition, personal data collected during negotiations with prospective tenant businesses shall only be used and retained for the purposes of letting and managing the industrial units.

Financial

49. The first phase business case methodology has been updated with the benefit of actuals, which coupled with inputs from the C+W Update Report and technical professionals, provides a robust platform to proceed with a second phase. Should construction achieve a surplus, this will be ring-fenced until such time as units are fully occupied and the development is completed.

Actions to be taken to implement the recommended decision(s)

Action	Responsible Officer	Deadline
As outlined within paragraphs 35 to 41.	Richard Horniman (Project Sponsor)	October 2024

Appendices

1	TeesAMP Phase 1
2	Teesside University Net Zero Industry Innovation Centre
3	TeesAMP Phase 2 Developable Area

Background papers

Body	Report title	Date
Executive	Tees Advanced Manufacturing Park – Delivery and Investment Enablement [Part A]	19 th December 2017
Executive	Tees Advanced Manufacturing Park – Delivery and Investment Enablement [Part B] <i>Exempt pursuant to Schedule 12A of the Local Government Act 1972 – Paragraph 3 – Information relating to the financial or business affairs of any particular person.</i>	19 th December 2017
Executive	Tees Advanced Manufacturing Park – Relocation of Option Site <i>Exempt pursuant to Schedule 12A of the Local Government Act 1972 – Paragraph 3 – Information relating to the financial or business affairs of any particular person.</i>	14 th July 2020

Body	Report title	Date
Executive	<p>Tees Advanced Manufacturing Park – New Site Development Options</p> <p><i>Exempt pursuant to Schedule 12A of the Local Government Act 1972 – Paragraph 3 – Information relating to the financial or business affairs of any particular person.</i></p>	23 rd March 2021

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