

FAREHAM

BOROUGH COUNCIL

Report to the Executive for Decision 05 July 2021

Portfolio:	Policy and Resources
Subject:	Variation to Construction of new units at Faraday Business Park, Daedalus
Report of:	Director of Planning and Regeneration
Corporate Priorities:	A dynamic, prudent, and progressive Council

Purpose:

To update the Executive on progress with the development of speculative industrial units at Faraday Business Park at Daedalus and to present options with regard to the provision of office accommodation in Units 15 and 16.

Executive summary:

At the 7 January 2019 Executive it was agreed to fund the construction of new industrial / business units at Faraday Business Park. The development consists of three buildings, with one of these divided into two to provide four units in total.

On 7 September 2020 the Executive considered a further report which assessed the impact of the Covid-19 pandemic on the prospects for the scheme, and it was agreed that the scheme should proceed.

Following the award of the construction contract, the build out is well underway with completion scheduled for Autumn 2021. Since that time updated marketing advice has been received and the construction sector has been impacted by the delay in steel production.

The above changes have triggered a review of the specification for the scheme and a recommendation that it be revised with all four units being provided with office accommodation to maximise the letting potential/income receipts from the development.

This report recommends a two-stage approach to the provision of office accommodation in Units 15 and 16 to mitigate the risk from potentially having void units.

Recommendation:

It is recommended that the Executive:

- (a) agrees to the two-stage process for providing office accommodation in Units 15 and 16 (set out in paragraphs 17 - 23 of the Executive Briefing Paper) and the required increase in the capital budget of up to £550,000.
- (b) approves a variation to the current construction contract, at an estimated cost of £165,000, to allow for the stage one office works to be undertaken.
- (c) grants delegated authority to the Director of Planning and Regeneration following consultation with the Deputy Chief Executive Officer and the Executive Member for Policy & Resources to award a contract(s) for the stage two office works, at an estimated cost of up to £385,000.
- (d) additionally, note that an additional capital budget of £50,000 is required to cover minor variations to the scheme following the award of the construction contract.

Reason:

To maximise the letting and income potential from the speculative development at the Faraday Business Park at Daedalus and to minimise risk.

Cost of proposals:

The capital budget for the development of industrial units at the Faraday Business Park will need to be increased by £600,000 up to a maximum of £5,600,000 to cover the cost of installing the frame, and potentially the subsequent fit out of office accommodation, together with minor contract variations.

Confidential appendices: By virtue of paragraph(s) 1 of Part 1 of Schedule 12A of the Local Government Act 1972.

Appendix A: Update and Advice from Joint Marketing Agents

Appendix B: Revenue Implications.

Background papers:

Reference papers:

Report to the Executive 07 January 2019 – Capital funding for the construction of industrial / business units at Faraday Business Park, Daedalus.

Report to the Executive 07 September 2020 – Covid 19 – Impact on Daedalus Investment Projects – Faraday Industrial / Business Units.

FAREHAM

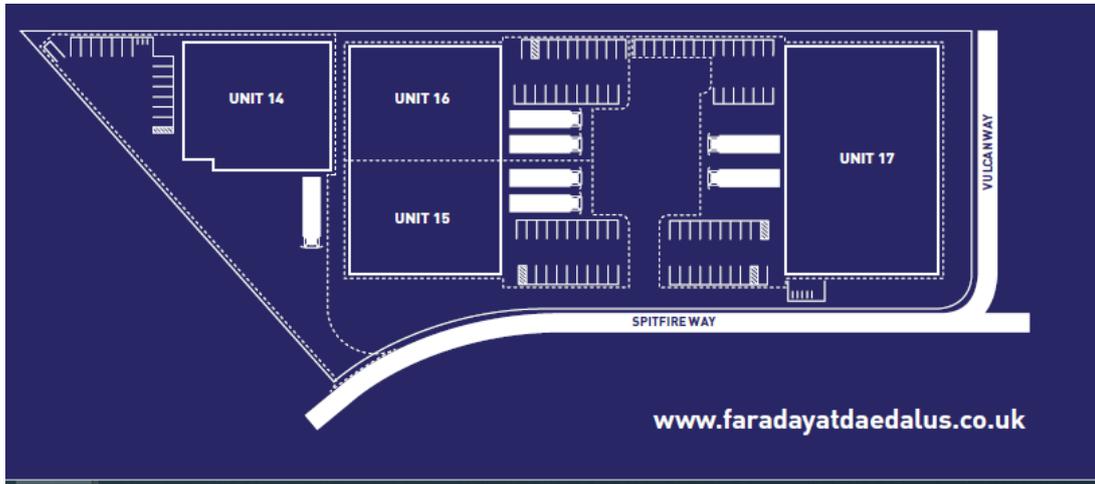
BOROUGH COUNCIL

Executive Briefing Paper

Date:	05 July 2021
Subject:	Variation to Construction of new Units at Faraday Business Park, Daedalus
Briefing by:	Director of Planning and Regeneration
Portfolio:	Policy and Resources

INTRODUCTION

1. At the 7 January 2019 Executive it was agreed to fund the construction of new industrial / business units at Faraday Business Park and that the appointment of a contractor for the development be delegated to officers following consultation with the Executive Member for Policy and Resources.
2. During 2020 the project was designed and tendered with the intention of awarding the contract as per the existing approval but, in light of the Covid pandemic, a further report was presented to the Executive in September 2020 advising that the Council's agents considered the fundamental market principles remained in place notwithstanding the Covid-19 impacts, and that a speculative scheme at Faraday Business Park would be successful and attract occupiers achieving a viable and profitable outcome.
3. A construction contract has since been awarded in accordance with the delegated authority and the development is progressing well with practical completion scheduled for autumn 2021.
4. The development consists of three buildings, with one of these divided into two to provide four units in total.
5. Units 15 and 16 are in one building in the centre of the development with Units 14 and 17 to either side and being individual buildings. Units 14 and 17 are being provided with offices/facilities, whereas Units 15 and 16 are not. An image of the proposed development and layout is provided below for context.



UPDATE

Economic Recovery and Market Review

6. The view provided by the marketing agents in September 2020 was that the commercial market would remain buoyant and they have subsequently advised that this remains the case with strong demand for this type/size of unit elsewhere in the region.
7. This view can now be confirmed with greater confidence following the appointment of Realest in addition to Lambert Smith Hampton as joint marketing agents for the development. The agents have confirmed the strength of the industrial sector evidenced by an increased number of property related transactions which have occurred since September 2020. This is combined with greater confidence that we are on the way out of Covid-19.
8. The market for speculative industrial business units is for a standard product that can be available for occupation without delay whilst a fit out is completed. Our agents have advised that 90% of tenants would anticipate offices and associated facilities and this is particularly relevant for the target sectors of aviation, aerospace engineering and advanced manufacturing industries.

Supply Constraints

9. The lead time to specify, tender and construct office accommodation has extended from 3 months to a minimum of 6 months and this period could be extended due to the current high demand for, and shortage of, construction materials. The marketing advice that has been received is that prospective tenants would not accept such a delay and would seek ready to occupy units elsewhere instead.
10. The updated advice from the joint marketing agents, combined with the current high demand for steel, has led a review of the development's specification and a recommendation that all four units are provided with office accommodation not two as originally specified.
11. A combination of these factors leads us to conclude it is prudent to recommend action to mitigate the potential delay to securing tenants at an early stage for all units.
12. A full copy of the updated marketing advice is at Appendix B

RISK ASSESSMENT

13. Following the receipt of recent updated market advice, it is evident that:
 - There is a risk that without offices/facilities Units 15 and 16 may be less attractive to potential tenants with consequent void periods and loss of rental income.
 - There are currently market shortages for steel which are leading to long lead times and potential delays to the future fit out of units, which tenants are unlikely to accept
14. If no action is taken to provide office accommodation in Units 15 and 16, the worst case scenario is that tenants are not secured and then the office accommodation would need to be provided retrospectively. The time taken to undertake the works is estimated at a minimum of six months therefore significantly extending the anticipated void period. This will result in lost rent and holding costs in addition to the capital cost of constructing the office accommodation. Please see Appendix B for additional detail in Table 1.
15. If the offices and facilities are installed additional rent will be secured due to an increase in the floor area. Furthermore, the latest expectations of the Marketing Agents on the rents that can be achieved for Units 15 and 16 have increased. Please see Appendix B (Table 2) for additional financial detail.
16. The risk of not installing offices/facilities is reduced if we sell the units. However, at this stage it is preferable to retain and let the new units to avoid fragmentation of the site, retain control over the future development of the Faraday site and to gain the benefit so the long-term rental income. We should not be closed to selling a unit or units, but initially the council should have a reasoned preference. Each market enquiry should be considered on its own merits.

RECOMENDATION

17. Based on the assessment of the current situation, the recommended way forward

to mitigate the financial risk from void units is to provide office accommodation via a two-stage process:

Stage One – Installation of the structure:

18. Within this stage, the current contractor would be instructed to install the basic steel frame, concrete floor, and staircase to provide the infrastructure for a future office fit out of Units 15 and 16.
19. The cost of this stage being £165,000

Stage Two – Fit out of the accommodation:

20. Following the completion of the basic infrastructure, the actual fit out to provide office accommodation, toilets and kitchenette facilities in one or both of the units, (if any) would be subject to the outcome of detailed negotiations with prospective tenants and the outcome of market testing. The fit out itself could be carried out either within the existing contract or via a separate contract arrangement.
21. The final decision would be taken being taken by the Director of Planning and Regeneration in consultation with the Deputy Chief Executive Officer and the Executive Member for Policy and Resources.
22. The estimated cost of stage two is up to a maximum £385,000 if both units are eventually fitted out with office accommodation by the Council.
23. The benefits of this approach are that:
 - The initial financial commitment would be an estimated total of £165,000 for the completion of the first stage. This would allow for further market testing before committing the funds for stage two.
 - The units would be more attractive / marketable to the target sectors such as aviation, aerospace engineering and advanced manufacturing industries.
 - The frame installation can be completed within the current construction contract, the programme for the subsequent fit out is reduced and flexibility is retained for prospective tenants to tailor the office accommodation to their needs.
 - This approach reduces the lead in time for the provision of offices by over 50%, thus helping to mitigate the short-term revenue risk.

FINANCIAL IMPLICATIONS

24. The Executive is requested to note that the project is currently forecast to be £50,000 over the approved capital budget of £5,000,000 due to minor contract variations and an increase in fees.
25. The current capital budget would also need to be increased by £550,000 to fund the recommended way forward to provide office accommodation in units 15 and 16 at the Faraday Business Park.
26. When this scheme was last brought to the Executive in September 2020, the payback period increased to 14 years from 12.5 years in January 2019. This accounted for revised assumptions due to Covid 19.

27. We have reviewed the modelling of the scheme accounting for a revised budget of £5,600,000. The payback period increases to 15 years using rents below the expectations of the Marketing Agents.
28. If the Marketing Agents most recent expectations are incorporated the payback period is in Year 14. More detail on the most recent rental expectations of the Marketing Agents on Units 15 and 16 is contained in Table 2 at Appendix B where they are compared against those used in the Covid 19 Review. You will note the increase and reasons for this. Finally, Table 3 at Appendix B presents the rental void modelling used in the Covid 19 review and that adopted now.
29. As noted above, if the offices and facilities are installed additional rent will be secured due to an increase in the floor area. Furthermore, the latest expectations of the Marketing Agents on the rents that can be achieved for Units 15 and 16 have increased. Overall, this increase is estimated at between £40,900 per annum to £46,900 per annum when compared to the Covid 19 Impact Report, presented to the Executive in September 2020.
30. Officers have considered options to make savings within the approved scheme and at this late stage we have just identified a small number of changes to finishes. No changes are proposed based on the small level of financial saving and the effect on the quality of the finished product.

CONCLUSIONS

31. The development at the Faraday Business Park is progressing well with practical completion forecast for October 2021.
32. Since the award of contract, based on updated marketing advice and the high demand and resultant lead times for steel, it is now advantageous to provide office accommodation in all four units.
33. The recommended way forward is to adopt a two-stage approach whereby the steel frame, concrete floor and staircase is provided within the current construction contract with the office fit out to be potentially carried out in a second phase. The second stage would be subject to negotiations with prospective tenants.

Enquiries:

For further information on this report please contact Steven Farndell, Estates Surveyor (Ext4587) or Ian Cousins, Property Manager (Ext 4835).