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Devolution and the role of Commercial Real Estate Development

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Faculty of Engineering and Environment
R3Intelligence

29th June 2016

PRACTICE & LAW BUSINESS RATES

Practice & Law

A recent flood of announcements concerning the devolution of government powers to local areas signals the general transfer of power from Whitehall to a quagmire. Devolution, growth and city deals are now the order of the day, with the Northern Powerhouse and Leeds Merit having been welcomed as a revolution in devolution for local authority working. These changes to the way governments in England have been broadly welcomed by city leaders and commentators alike as an opportunity for local areas to exert control over their destiny and stand on their own two feet.

So far, there has been very little debate surrounding what these changes mean for the commercial property sector. This article is particularly timely with respect to the chancellor's announcement, at the Conservative Party Conference, of the full localisation of business rates. The statement took many by surprise (the SNP quickly announced similar proposals in Scotland) and initially received considerable attention. After a brief spate in media coverage, however, the matter has subsequently dwindled to a (disappointing) level.

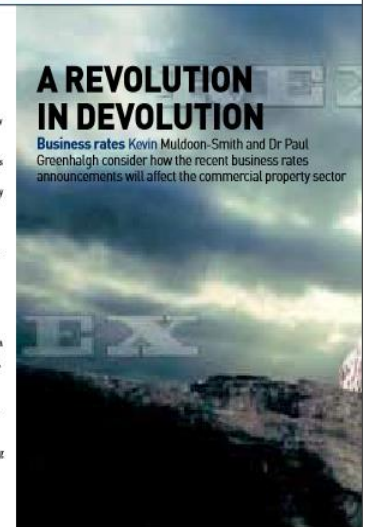
Make no mistake, following devolution, local business rates, and by extension the performance and potential growth of local commercial real estate markets, will become a central concern not only for local authority financial planning and investment but the wider business sector and local economies.

The reality of the situation is currently difficult to fathom ahead of the impending public spending review due at the end of this month. However, what is possible is the recent exposure of this traditionally obscure issue and the opportunity for debate. This article reflects on some of the uncertainties, assumptions and contradictions in the recent business rates announcements and the potential challenges and opportunities for public sector providers and the commercial property sector.

Commercial real estate
The original business rate revision

A REVOLUTION IN DEVOLUTION

Business rates Kevin Muldoon-Smith and Dr Paul Greenhalgh consider how the recent business rates announcements will affect the commercial property sector



Introduction

A whirlwind tour of R3 Intelligence and our recent work:

- Where the project originated
- How we have done it
- What we have produced
- Why it is important

Reason for producing this summary:

- Disseminate preliminary analysis and findings
- Demonstrate the synergy between commercial real estate and devolution
- Offer opportunity for feedback and suggestions as to how we can support landlords and developers in the devolution revolution

Project Evolution

- Previous research regarding commercial real estate filtering, chaining, displacement and resilience (Greenhalgh 2003, 2008, Greenhalgh and King 2010, 2013).
- Highlighted gap and potential for hybrid property market data models.
- Led to PhD studentship (Dr Kevin Muldoon-Smith) and the creation of a multi criteria real estate model of England and Scotland using Valuation Office Agency and National Business Rate Returns.

Method (Data and Filtering)

- The model of commercial and industrial property can be drilled down into the individual hereditament or aggregated and up-scaled to property sector (including relative homogeneity).
- The presentation of our data is flexible (descriptive, trend, statistical, and spatial/GIS) and has the potential to be further enhanced with additional data sets such as IMD, Local Government Spend, Business activity etc

Our data base contains:

	(millions)	(Billions)
■ Office space:	92m sq m	1bn sq ft
■ Industrial space:	323m sq m	3bn sq ft
■ Retail space:	181m sq m	1bn sq ft

Initial Analysis

- Office vacancy time bomb
- Citibase Ltd: Survey of secondary office vacancy in the UK
- Spatial Analysis/GIS modelling of:
 - Tyne and Wear
 - Tees Valley
 - Leeds
 - Croydon

Taking Stock: secondary opportunities and the agile future

An academic research survey conducted by Northumbria University
Published August 2015



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NEWS SPACE EQUIVALENT TO DOUBLE LEEDS' OFFICE STOCK IS SITTING EMPTY

£3BN OFFICE TIMEBOMB

30,000

POTENTIAL NUMBER OF HOMES

HIGHEST RENT LEADERS (sq ft)

MANCHESTER	£2.7M
LEEDS	£2.5M
LONDON	£2.1M
NEWCASTLE	£1.9M
CROYDON	£1.8M

MOST VACANT SECONDARY AND TERTIARY SPACE

MANCHESTER	1,994,500 FT
LEEDS	2,392,500 FT
NEWCASTLE	26,500 FT
LONDON	1,794,500 FT
MOTT MACDONALD	1,594,500 FT
SOUTHAMPTON	1,394,500 FT
MULTI CENTRES	1,194,500 FT
CARDIFF	994,500 FT
SEASIDE	994,500 FT

VACANT SPACE

SUMMARY 1.1M SQ FT
FROM 1.5M SQ FT
SECONDARY 10.1M SQ FT

The vacant stock could prove attractive to investors looking to take advantage of government's relaxed planning laws to convert offices to homes. Use of permitted development rights in London has seen applications for nearly 5,000 homes over the past year (p27).

The vacant regional offices have the potential to be redeveloped as circa 30,000 homes. Muldoon-Smith said that of the 2,150 vacant secondary properties, 44% of the space was in 100 centrally located properties, which could be seen as "urban stock pickers, directing intervention where it is most needed".

"Many of these properties are appropriate for adaptive reuse."

Muldoon-Smith said: "This is a consequence of a major structural change. Office demand has changed due to working practices, technology, downsizing and the recession, but this supply has not been adapted because of its restrictive functional design."

The study analysed 2010-14 business rate returns and valuation office data.

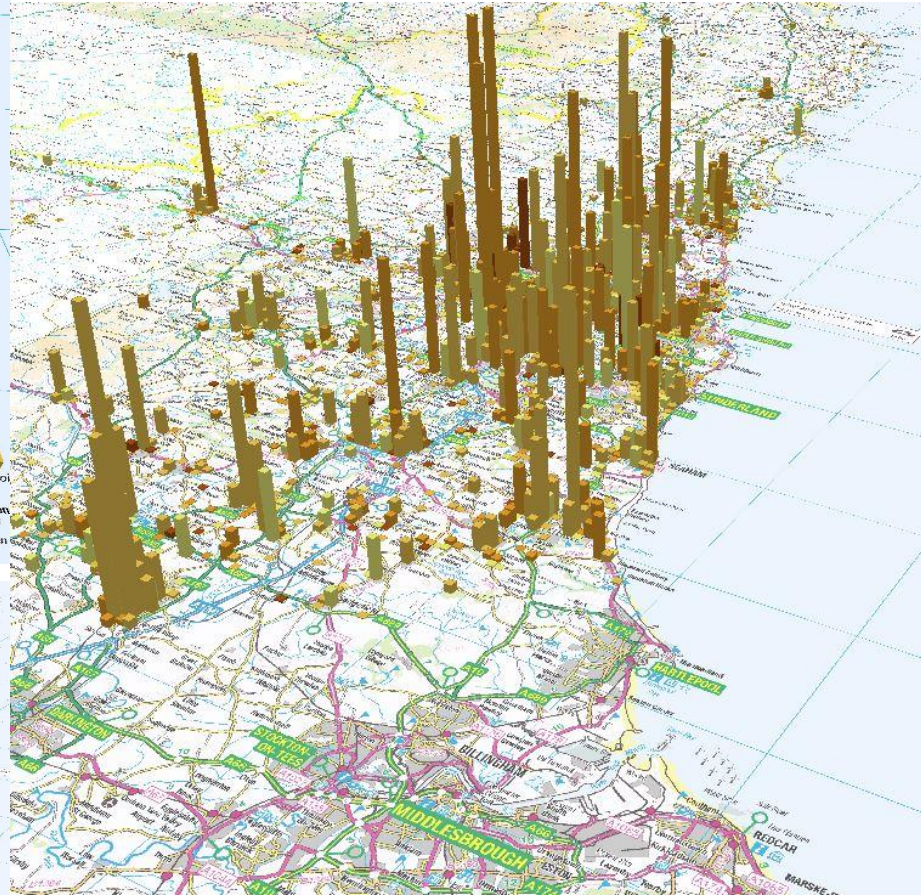
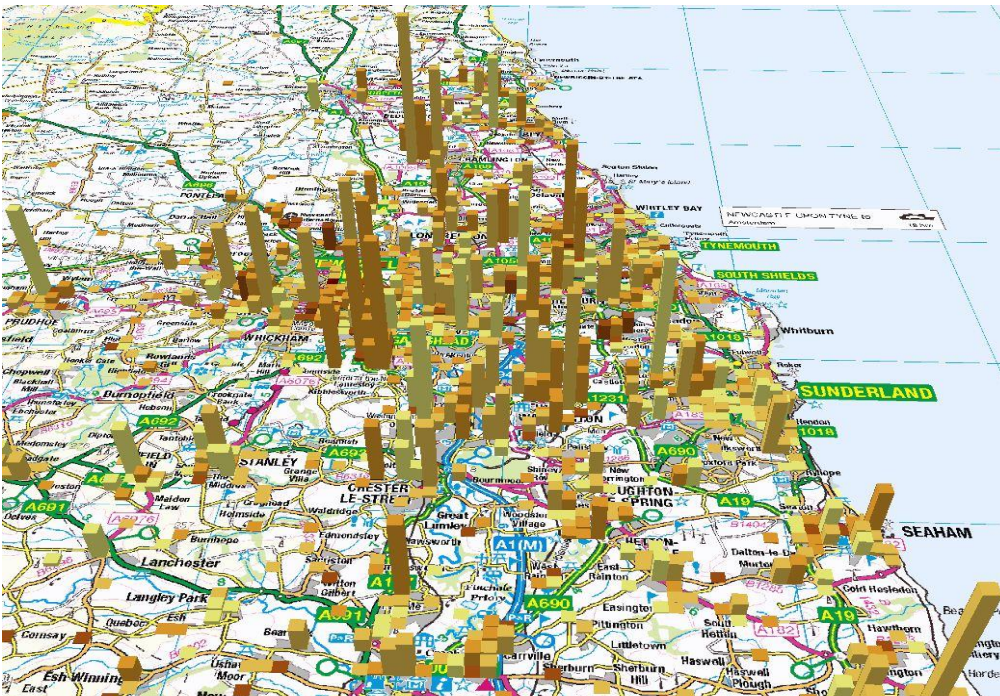
because of their underlying land value and potential rental value, a win-win situation," he added.

A Taxpayers Alliance investigation last year (10 March 2014, p26) revealed that the industry pays around £1.5bn in empty property rates.

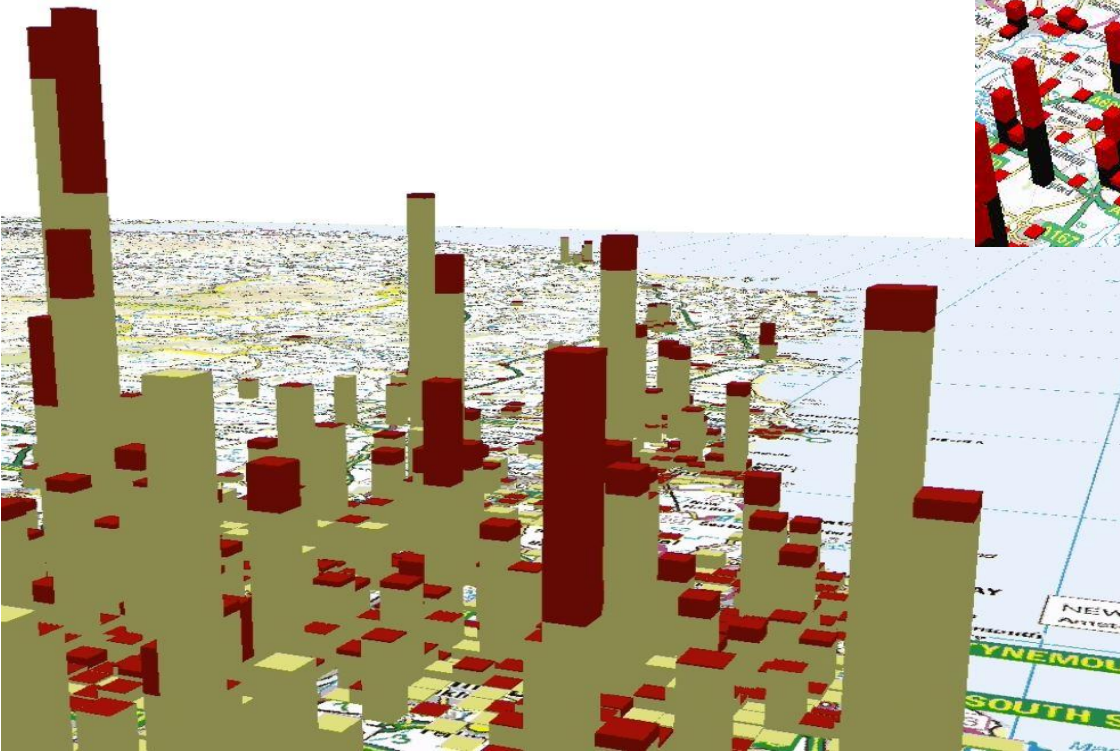
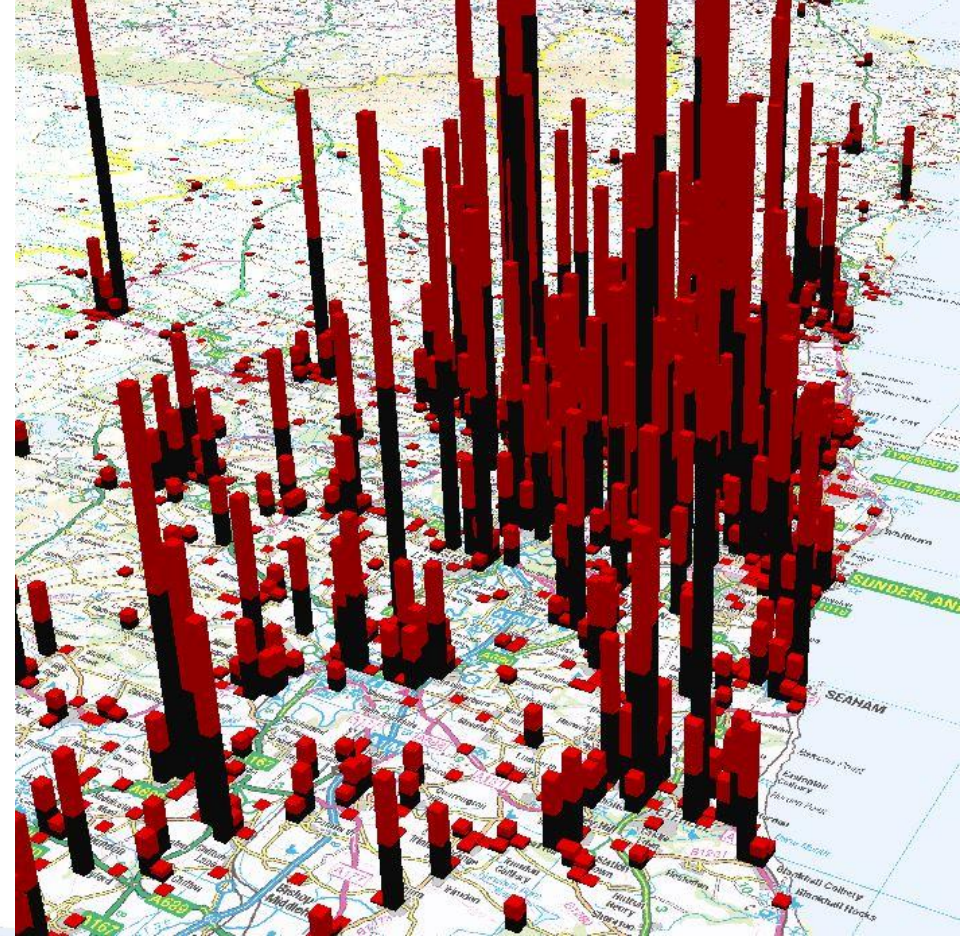
British Property Federation chief executive Liz Peace reiterated her call for reform of empty rate policy calling for the tax money to instead be invested in bringing the vacant office highlighted in this latest study back into productive use.

She said: "Many of these buildings will be crying out for redevelopment - not refurbishment - this is economically productive activity that generates jobs and helps to regenerate urban areas, and should be encouraged, not punished, by the tax system."

Manhattan on Tyne and Wear

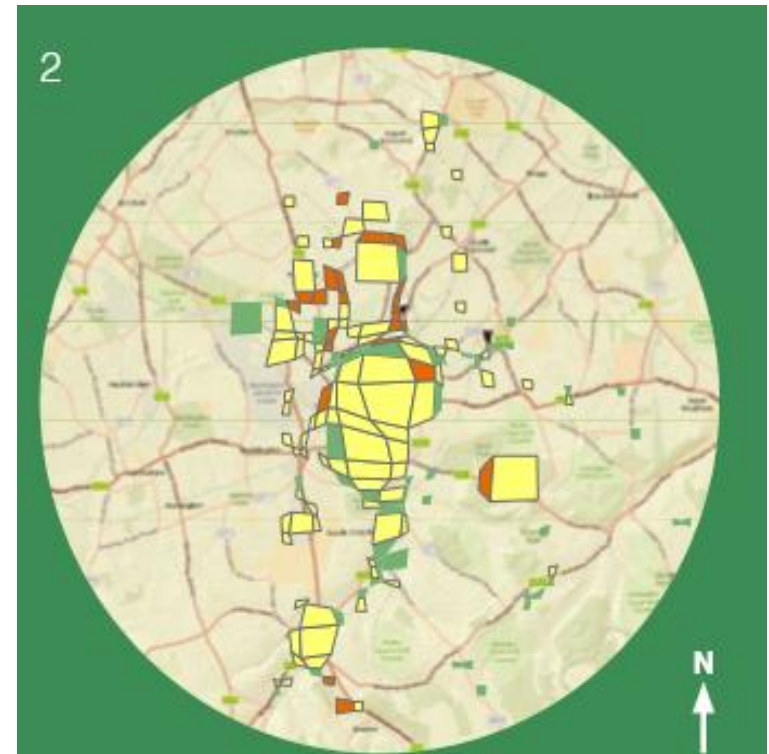


Stock Efficiency: a GIS model of commercial & industrial stock and vacancy in Tyne and Wear



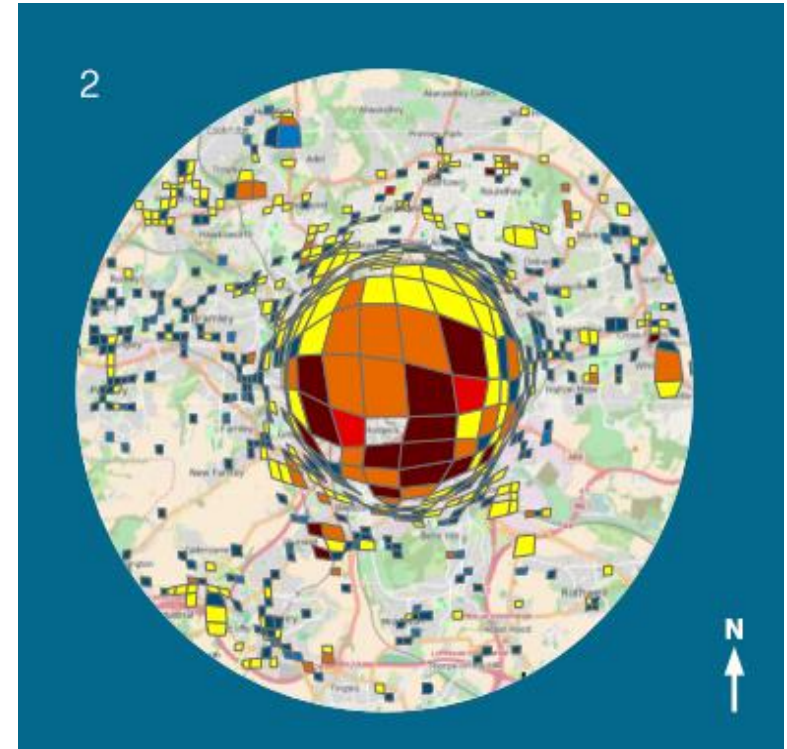
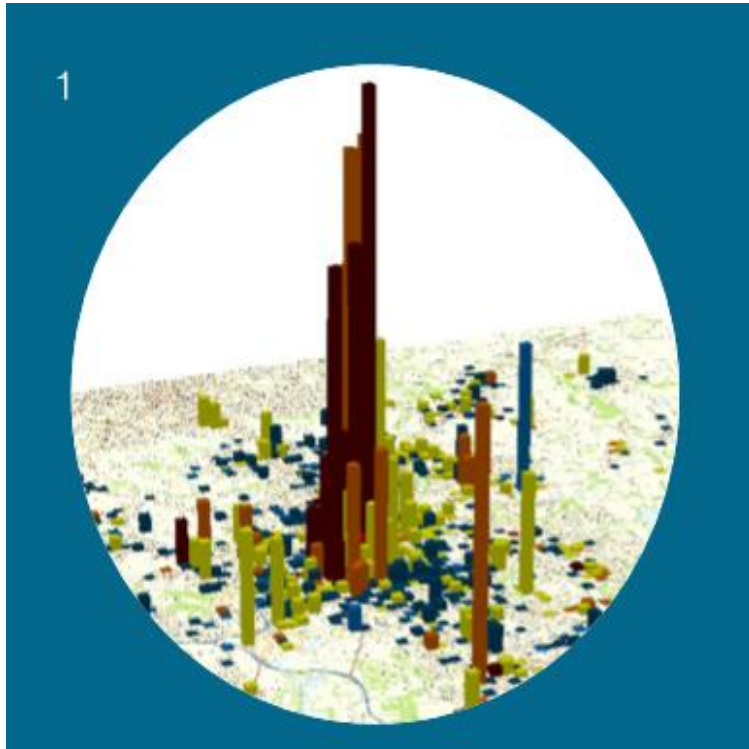
<http://r3intelligence.co.uk/>

The Croydon Office Market



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The Leeds Office Market



Current Position

- We now have a fully functioning multi-criteria model of the commercial real estate market in the UK - this has never been done before.
- Alongside the perennial importance of 'location, location, location' we now have 'evidence, evidence, evidence.'
- We have the ability to apply this methodology to any geographical area in England, Wales and Scotland.
- The last dataset provided by the Government regarding property market vitality was published in 2005 (a local authority scale estimate); it is still being used to inform current policy initiatives such as the recent permitted development right rule changes regarding office to residential conversion.

Subsequent research

- Our model is based on national property valuation and tax information
- This has allowed us to explore and feed into the current devolution and fiscal decentralisation debate.
- We have submitted and subsequently been called as expert witnesses to:
 - All Party Parliamentary Group (APPG) round table on Reform, Decentralisation and Devolution in the UK, and
 - Communities and Local Government (CLG) Select Committee review of business rate retention.

Some questions?

- Devolution is happening but what are its consequences for the region?
- Is the 'Northern Powerhouse' more than just a brand?
- Devolution is underwritten by business rate retention and that means the performance of existing commercial property and the development of new property stock
- How will the stock of commercial and industrial property and supply of new build influence local government funding in the region?
- There is much confusion and little detail about financialisation of real estate - we hope to shed some light on these matters

Why is this important?

- Towns and cities need to make best use of existing property and plan new development accordingly – currently there isn't any evidence base!
- Our model provides evidence for:
 - More efficient land use planning
 - Economic development strategies
 - Business rate retention planning
 - Monitoring and simulation of contemporary methods of urban intervention such as:
 - Tax Increment Financing (general and new development deal),
 - Enterprise Zones
 - other retained business rate models such as Accelerated Development Zones
- One way or another, public sector service provision is now pegged against the performance of commercial real estate; we can monitor this performance and direct its potential improvement.

Opportunity knocks: Not just about LAs

- No representation from landlord or development sectors into these enquiries – missed opportunity!
- Did you know that Local authorities make more money out of Empty Property Rates than business activity? – opportunity to reform Empty Property Rates
- Real estate development funds devolution – opportunity for landlords and developers to take centre stage and lead the devolution debate
- How will business occupiers and small businesses be affected by the way property markets respond to challenges?

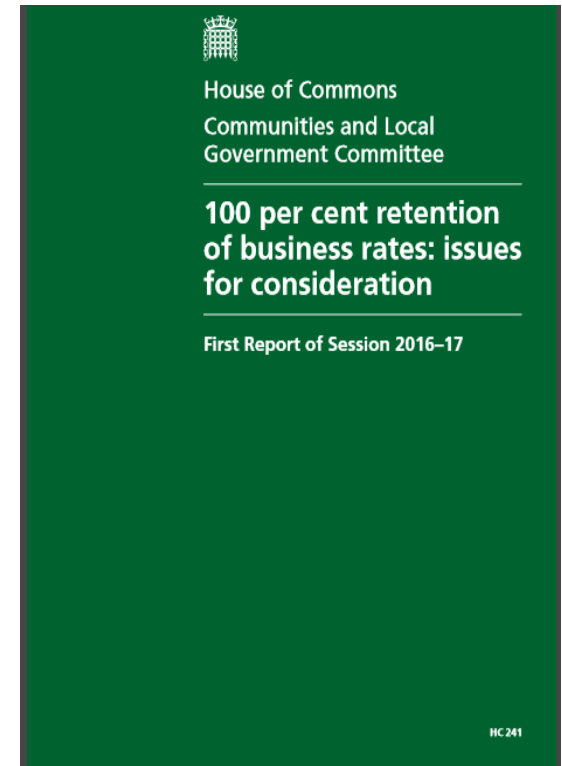
and finally...

- What do you think?
 - First impressions
- What can else could we do?
 - Identify potential to extend application
- Have we missed any tricks?
 - Identify new opportunities
- Let us help you – give us access to your data

Any thoughts to:

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R³ I N T E L L I G E N C E

R I G H T S P A C E R I G H T P L A C E R I G H T T I M E

R3intelligence is dedicated to supplying high quality impartial commercial real estate research and advice.

Request an exploratory meeting with either Dr Paul Greenhalgh or Dr Muldoon-Smith

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