



BIG Things in SMALL Boxes

The industry-leading report on the Industrial & Logistics small to mid-box property market.

November 2024





Contents

Foreword.....	p.4
Executive Summary	p.5
Defining the Diverse Sub 100k sq ft I&L Sector	p.6
The Economic Background	p.7
The Role of the I&L Sector for Economic Growth	p.8
The Supply Shortage in the Small to Mid-box I&L Sector.....	p.10
Unlocking Suppressed Demand	p.12
The Affordability Crisis.....	p.13
The Regional Imbalance	p.14
Innovation Challenges in the UK from Start-up to Scale-up ...	p.16
The EPC Cliff Edge.....	p.18
Sustainable Energy Potential	p.20
Conclusion.....	p.22
About Potter Space	p.24

Foreword: Boosting the Economy with BIG Things in SMALL Boxes



Jason Rockett
MD, Potter Space

Potter Space has long believed that the small- to mid-box market is the unsung hero of I&L property, with the power to unlock large scale economic growth. So why is it facing so many challenges in supporting growth?

Welcome to our market leading research BIG things in SMALL boxes 2024. This is our third annual edition, focusing on the small to mid-box (sub-100k sq ft) Industrial & Logistics (I&L) property market.

Commissioned by Potter Space and conducted by Savills, BTISB provides crucial insights into this often overlooked but highly significant economic segment for industry stakeholders, policymakers and businesses.

The small to mid-box I&L sector is an economic powerhouse, contributing £124 billion GVA per annum to the UK economy. A surprising 95% of units in the I&L property market are small to mid-box, with 2.1 million people employed in them - 55% of the I&L sector employment.

Despite a stagnant UK economy over the last decade, the I&L sector displays many signs of growth. Job growth¹ and productivity² are significantly higher than other sectors, and the future trends predict further growth due to more people needing more goods and the growth of ecommerce³.

In our latest report, we share the continuation of themes from previous reports and shine a light on some important new findings:

The under supply of quality stock into the market has been the main finding since its launch. Businesses are “making do” with the space they occupy as a result, suppressing their growth. This level of suppressed demand is calculated to be 38% UK-wide and requires 63 million sq ft of sub-100k sq ft space to unlock it. Sadly, it remains a theme this year despite the opportunity that addressing it presents. Building business, the space it needs to grow, could create 94,000 jobs and directly contribute £3.2 billion and indirectly contribute £2.7 billion of GVA into the UK economy per annum.

The 2024 report also highlights the productivity gap opening in the UK; with smaller companies unable to find the space they need to grow. The UK is a hotbed of innovation; the start-up rate here is the second highest globally⁴, but a failure to effectively scale up operations means there is also a very high failure rate. In 2022, business deaths outnumbered business births for the first time since 2010⁵. Lack of availability of suitable property is a significant barrier to business growth and realising the value of their innovation.

This year, we also reveal the impending EPC cliff edge. Government regulations on EPC – whilst important environmental measures, potentially exclude up to 85% of current stock from being let due to an inability to meet EPC level B by 2030. It's a largely unreported ticking time bomb.

The solutions to these and the other issues highlighted in BTISB 2024 revolve around planning reform, support for sustainable stock and increased industry collaboration. Each are huge topics which require significant and urgent attention from industry and government.

At Potter Space, we want BTISB to be a catalyst for change and the unlocking of opportunity. We want to bring industry stakeholders, policymakers, the media and businesses together to debate and take action.

Over the coming weeks, we will be releasing these findings through the media, our website and our social platforms.

Thank you for reading and welcome to the debate.

¹ ONS ASHE, Workforce Jobs by Industry

² ONS Output per hour, ONS Input-Output Tables 2019

³ Statista, DfT, MDS Transmodal, Boeing, Savills, Pitchbook

⁴ Global Startup Ecosystem Index Report 2024 <https://www.startupblink.com/startup-ecosystem/united-kingdom>

⁵ Statista, 2023 <https://www.statista.com/statistics/285285/number-of-new-enterprises-in-the-united-kingdom-uk/>

Executive Summary

The small to mid-box market faces significant challenges whilst holding immense potential for driving UK economic growth. This report illuminates the sector's current state, its challenges, and its pivotal role in addressing key economic issues. It also makes recommendations about the best path forward.

Key findings

1. Supply and Demand Imbalance

- A persistent shortage of suitable premises has suppressed demand by 38% across the country, a shortfall of 63 million sq. ft over the last decade.
- Addressing this imbalance could create up to 94,000 jobs and contribute £3.2 billion in direct GVA annually to the UK economy.

2. Support for Productivity, Innovation and Growth

- The UK ranks 2nd in the Global Innovation Index, however, also has one of the highest company death rates across Europe as we are not supporting these companies to grow.
- Providing suitable and affordable premises would enable the transformation of intellectual and creative outputs into tangible, market-ready products and sustainable businesses.

3. The EPC Cliff Edge

- 85% of existing inventory is at risk of becoming unlettable by 2030 due to new energy efficiency standards.
- The sector faces a dual challenge of upgrading existing stock while meeting growing demand for new, sustainable spaces.

4. Affordability Crisis

- Rapidly rising operational costs, particularly in rates, rent and energy, threaten the viability of many I&L businesses, especially SMEs.
- This crisis not only impacts individual companies but poses risks to supply chain efficiency and overall economic resilience.

5. Regional Development Opportunity

- The diverse locational requirements of small to mid-box occupiers present a unique opportunity to drive more geographically balanced investment.
- This could additionally address regional inequalities in wages and productivity, particularly give the above average salaries in the I&L sector.

6. Sustainable Energy Potential

- The sub-100k sq. ft I&L sector has the capacity to generate up to 11.2 TWh of energy from rooftop solar, equivalent to powering 4.3 million homes.
- This showcases the sector's potential role in the UK's sustainable energy future.

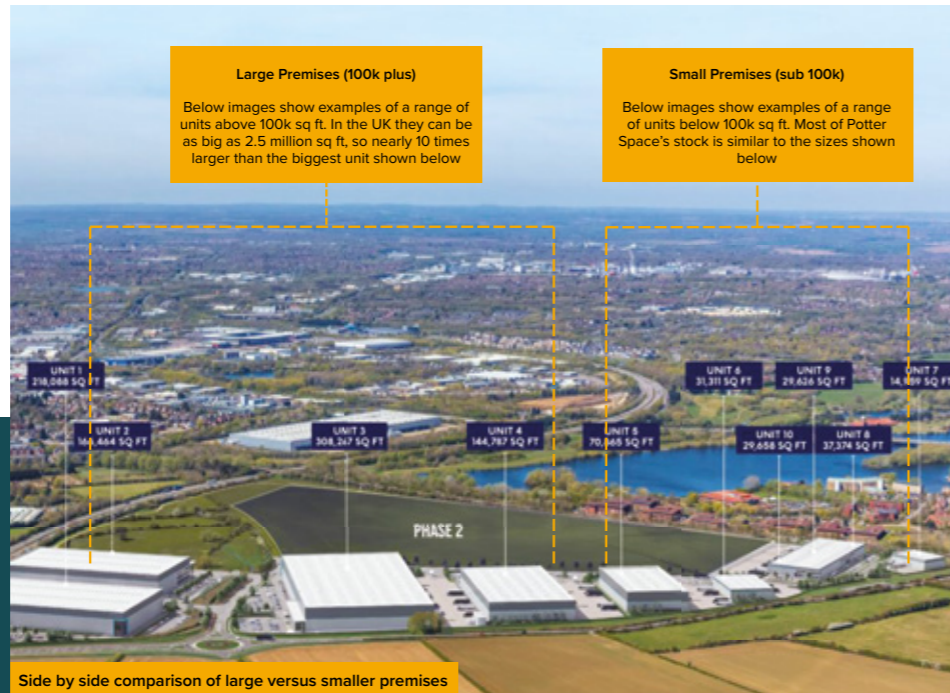
The small to mid-box I&L sector is not just a component of the UK's economic infrastructure; it is an engine for growth, innovation, and regional development. By addressing these challenges and capitalising on the sector's potential, the UK can unlock significant economic benefits, drive sustainable development, and create a more resilient and balanced economy.

Implications and Recommendations

- Planning Reform:** Planning policy and speed of decision making requires reform to support and accelerate the development of small to mid-box I&L spaces.
- Investment in Quality Premises:** Create targeted incentives for developers and investors to focus on the sub-100k sq ft market.
- Energy Efficiency Support:** Develop programmes to assist landlords in meeting new energy efficiency standards.
- Regional Strategy:** Implement a coordinated approach to leverage the sector's potential for addressing regional economic disparities and support leveling up.
- Sustainability Integration:** Encourage the integration of sustainable technologies, such as solar panels, in new and existing I&L spaces.
- Electrical Infrastructure:** All developers are struggling to bring schemes forward due to capacity issues in the grid. The grid requires enhancement to enable new schemes to come forward efficiently.

Defining the Diverse Sub 100k I&L Sector

The small to mid-box market (sub-100k sq. ft) can be characterised by the diversity of its occupiers, building types and locations. This diversity contributes to its resilience and importance within the broader I&L sector. In the face of challenging economic conditions, small to mid-box warehousing boasts a occupier diversity that other market segments would struggle to match.



Side by side comparison of large versus smaller premises

Image source: <https://www.plproperty.com/sites/plp-milton-keynes>

The Economic Background



This report explores the I&L sector's relationship with the UK economy. The detailed economic analysis we undertook (available on request) leads to the following conclusions and observations:

- The UK has seen very **limited growth in productivity** since the 2008 financial crisis. The lack of investment in the wake of the crisis, austerity measures to limit government debt, and negative shocks such as the COVID pandemic and Brexit have all prevented a return to positive growth, especially when compared with the US and the Eurozone (figures 2.1, 2.2 and 2.3).
- The UK has a **heavily regionalised economy**. This is recognised by the UK government in the Levelling Up white paper. The East, South East and London have significantly higher levels of investment into research and development. When examining economic output, only London and the South East have higher than average productivity and wages.
- SMEs employ more than 53% of people in the UK, leading many to characterise the UK as an **SME economy**. However, smaller firms are less productive and generate less turnover per employee. This lack of productivity is to be expected within small and start-up firms, as they seek to develop products and services to monetise at scale.
- The UK is **not successfully supporting small business owners** to scale up and move from research and development to production. The data shows that the UK produces world-leading research, which doesn't translate into economic productivity. Part of the reason for this is a lack of good quality, affordable I&L space.

Clearly there are a host of factors affecting the UK's stagnant economy but this insight suggests that levelling out regional bias and supporting businesses on their growth journey could facilitate wider economic progress.

Diverse occupiers

While transportation, warehousing, and retailers dominate the big-box market, sub-100k sq. ft offers a more balanced profile of occupiers across the likes of manufacturing, wholesale and professional, scientific and technical services, as well as miscellaneous sectors including construction, recreation and healthcare (figure 1).

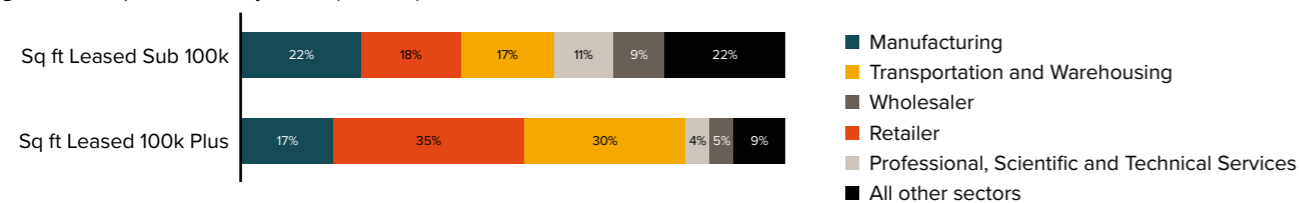
Diverse building types

Occupiers in this market have varying needs from their buildings. This begins with size – there is of course a significant difference between a 10k sq. ft warehouse and a 100k sq. ft one – and extends to facilities such as 24-hour access, generous loading space, flexible layouts, temperature regulation, security and parking.

Diverse locations

Small to mid-boxes occupy a variety of locations to suit client needs. That might include access to major transport networks (regional distribution centres), proximity to conurbations (last mile delivery hubs), or convenient commuter distance to talent or educational centres (R&D facilities). This creates demand for premises in city centres, on edge-of-town industrial parks and along major motorways.

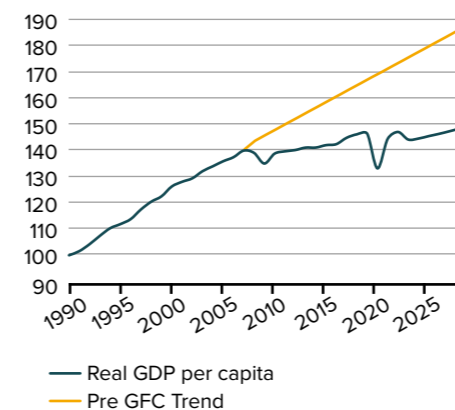
Figure 1 Floorspace leased by sector (2019-23)



Source: Savills analysis of Costar data

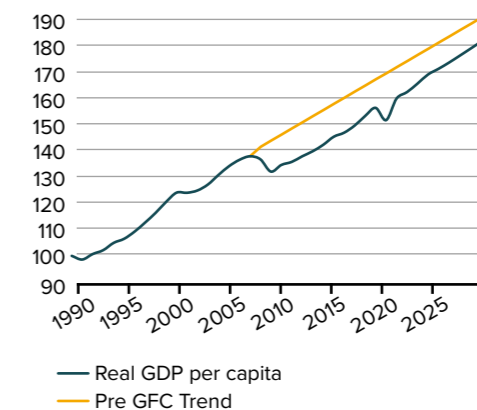
Economic growth has almost flatlined in the UK since the 2008 global financial crisis

Figure 2.1 Growth in Real GDP per Capita - UK



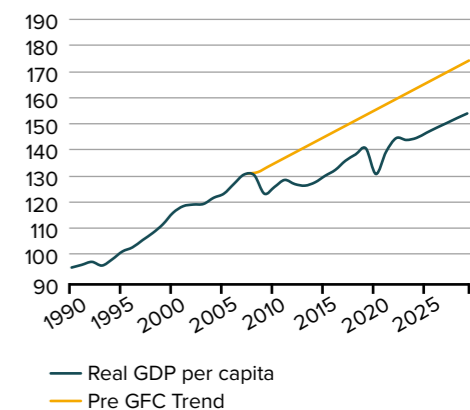
The US has returned to similar levels of growth as seen before the 2008 global financial crisis

Figure 2.2 Growth in Real GDP per Capita - US



Where the Eurozone was growing slower than the UK and US, it has returned to a comparable level

Figure 2.3 Growth in Real GDP per Capita - Eurozone



The Pivotal Role of the I&L Sector for Economic Growth

A Facilitator of Growth

The I&L sector plays a pivotal role in the UK economy, serving as a barometer for overall economic health and a catalyst for growth across various industries. By looking at the sector's economic landscape, highlighting its resilience, evolution, and potential for future expansion, with a particular focus on the often-overlooked sub-100k sq. ft market, the vital role that this sector plays becomes apparent.

Sector Growth and Productivity

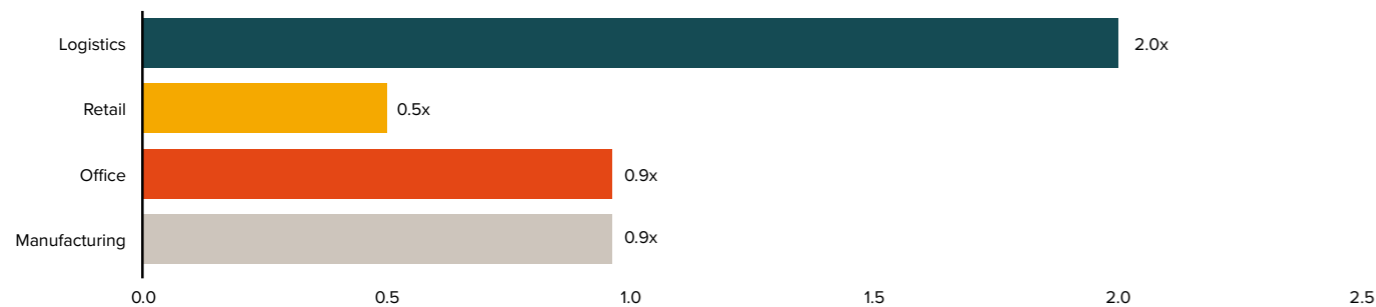
- The logistics sector is the fastest-growing segment of the economy, with job growth of 26% between 2015 Q1 and 2024 Q1, compared to 10% across the entire economy.
- Manufacturing productivity is 11% higher than the overall economy, with output per hour growing 61% between 1998 and 2019, versus 26% across all industries.
- The logistics sector's indirect Gross Value Added (GVA) is 2.0 times higher than its direct GVA, outperforming other sectors in economic ripple effects (figure 3.1).

Evolving Workforce

- Job roles are shifting towards higher-skilled positions in management, professional, and associate professional occupations (figure 3.2).
- Increasing collocation of office and warehousing staff is diversifying the skill set within I&L facilities.
- Logistics and manufacturing offer higher median wages than the all-sector average, with logistics entry-level jobs paying 47% more than comparable roles in other sectors.

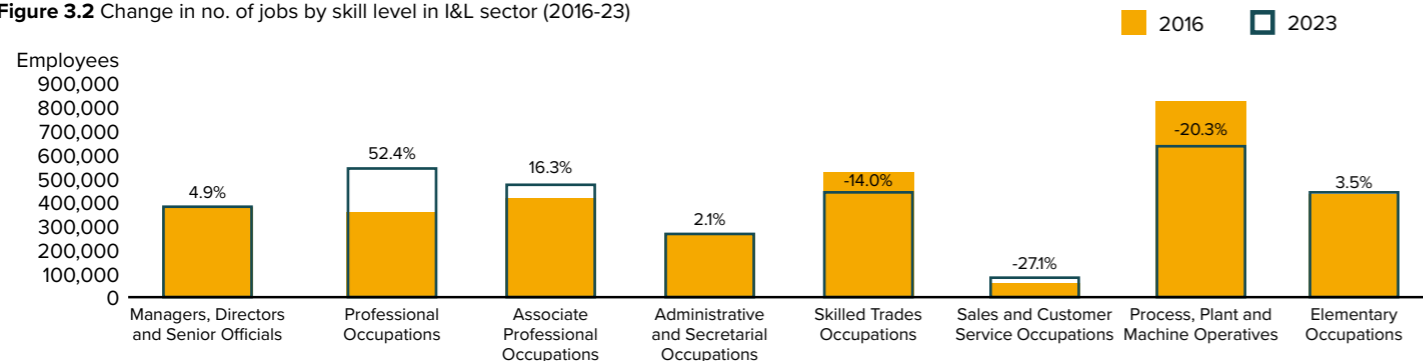
The logistics sector has the biggest multiplier effect of any industry

Figure 3.1 Indirect GVA by sector



Jobs in the I&L sector have become higher skilled in recent years

Figure 3.2 Change in no. of jobs by skill level in I&L sector (2016-23)

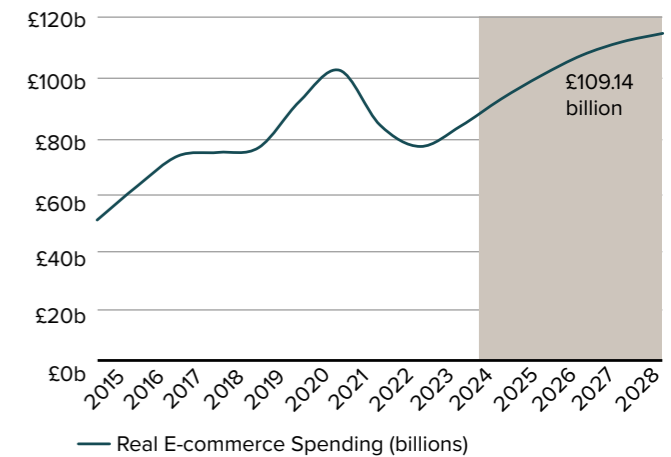


The Driving Factors for Increased Demand

- **E-commerce expansion:** Online spending has grown substantially over the past decade and is forecast to reach £109 billion by 2029, necessitating more I&L space for fulfilment and distribution.
- **Housing development:** The new Labour government's commitment to increase housebuilding, targeting 1.5 million homes in the next five years, is set to create additional demand for construction-related logistics and storage. It is expected that for every new home built, 74 sq ft of warehousing is required. So demand is forecast to increase on this basis alone.
- **Trade flow increases:** As the volume of goods entering and leaving the UK rises, so does the need for I&L floorspace to sort, package, and distribute these items.
- **Venture capital investment:** Between 2019 and 2023, £229 billion of venture capital was invested in emerging sectors related to I&L, including climate tech, mobility tech, and supply chain tech. Notably, the sub-100k sq. ft market plays a crucial role in supporting these startups through their development and scaling stages.

The value of online spending is forecast to rise

Figure 4 Past and forecast online spending growth in the UK (2015-29)



Role of Sub-100k sq ft Market

To examine the role of the small to mid-box market within this wider ecosystem, it's important to consider what it can offer the wider economy:

- Varied and resilient customer base.
- Diverse geographical footprint.
- Flexible product offering.
- Supports businesses throughout their growth journey.
- Ability to cater to emerging sectors attracting investment.

Size of the Small to Mid-box Market

- **95%** of units in the I&L property market are small to mid-sized units.
- The sector delivers **£124 billion** Gross Value Added (GVA) into the UK economy per year – that's 7% of the total economy.
- It provides employment for **2.1 million** people across England.
- More than **55%** of jobs in the I&L sector are employed in small to mid-sized units.
- **13,000** people start apprenticeships in these spaces each year.

While the I&L sector as a whole supports the economy, the sub-100k market plays a unique and essential role to support burgeoning businesses and sectors with enormous potential for growth, creating a knock-on effect of prosperity.



Supply Shortage in the Small to Mid-box I&L Sector

The UK has grappled with persistent supply constraints over the past decade, with the small to mid-box market bearing the brunt of this shortage. This imbalance between supply and demand has far-reaching implications for businesses and the broader economy, creating a landscape of missed opportunities and financial challenges.

Development Trends and Market Dynamics

When prime development land becomes available, it is swiftly transformed into high-quality units. However, the past decade has witnessed a marked preference for big-box units, driven by robust demand and investor inclination. These larger units offer compelling advantages: lower build and management costs, coupled with occupiers boasting stronger financial covenants. Consequently, larger units have emerged as the more viable option for developers and investors alike.

This shift in focus has left the sub-100k sq ft market comparatively underserved (figure 5.1). Despite its own robust demand, this segment has seen significantly less supply development, creating a widening gap between available space and market needs.

Market Constraints and Industry Benchmarks

Industry research suggests that an 8% availability rate represents the equilibrium point for the I&L sector. When availability dips below this threshold, the market enters a supply-constrained state, presenting significant challenges for potential occupiers seeking suitable space. This scarcity not only limits business growth but also fosters an environment of intense competition for available units. The small to mid-box market currently sits around 4.9% demonstrating constrained supply (figure 5.2).

Financial Implications and Market Pressures

The supply shortage has triggered a disproportionate surge in rental growth when measured against inflation. Over the past decade, rental rates have skyrocketed by 87%, vastly outpacing the 29% increase in inflation. This disparity poses significant challenges for occupiers in search of cost-effective units, potentially impacting their operational efficiency and bottom line.

The persistent supply shortage in the small to mid-box I&L sector signifies a missed opportunity for economic growth and business expansion across the UK. The need for targeted development and strategic planning in this sector has become critical.

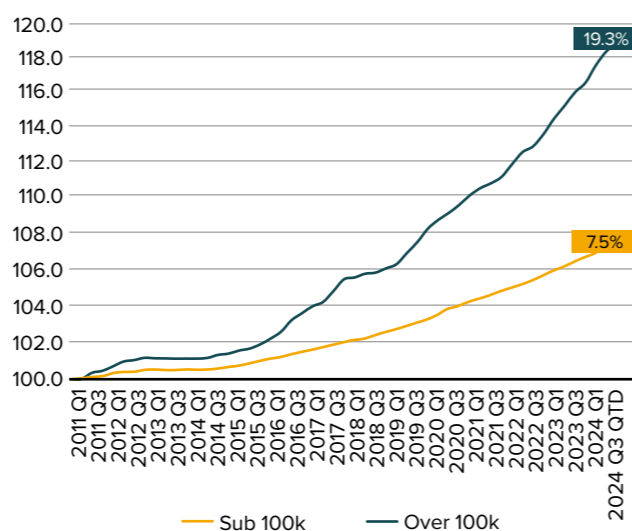
Impact on Businesses

The repercussions of this supply shortage are significant. Many businesses find themselves unable to secure the space necessary for growth and expansion.

This phenomenon is not isolated to a single region; it permeates the entire UK landscape (figure 5.3). Particularly hard-hit are areas such as the East Midlands and East of England, where suppressed demand soared to over 60% compared to realised demand. These figures paint a stark picture of lost opportunities and stifled business growth across the nation.

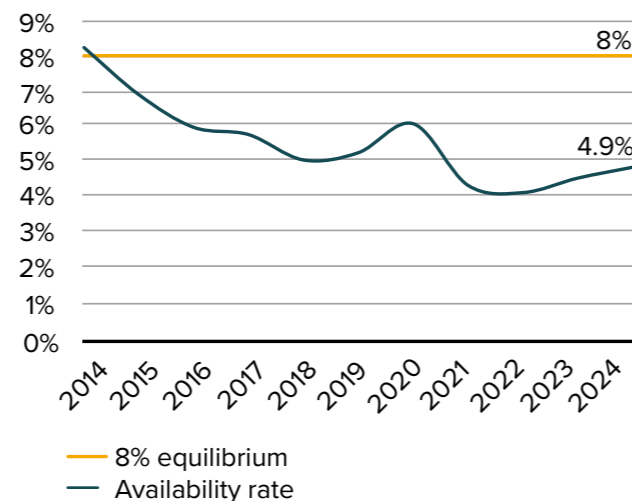
Development of premises over 100k sq ft have outpaced the sub 100k sq ft market

Figure 5.1 Indexed inventory growth - sub 100k sq ft market vs. 100k sq ft plus market (2011-24)



Availability has been falling over the last decade

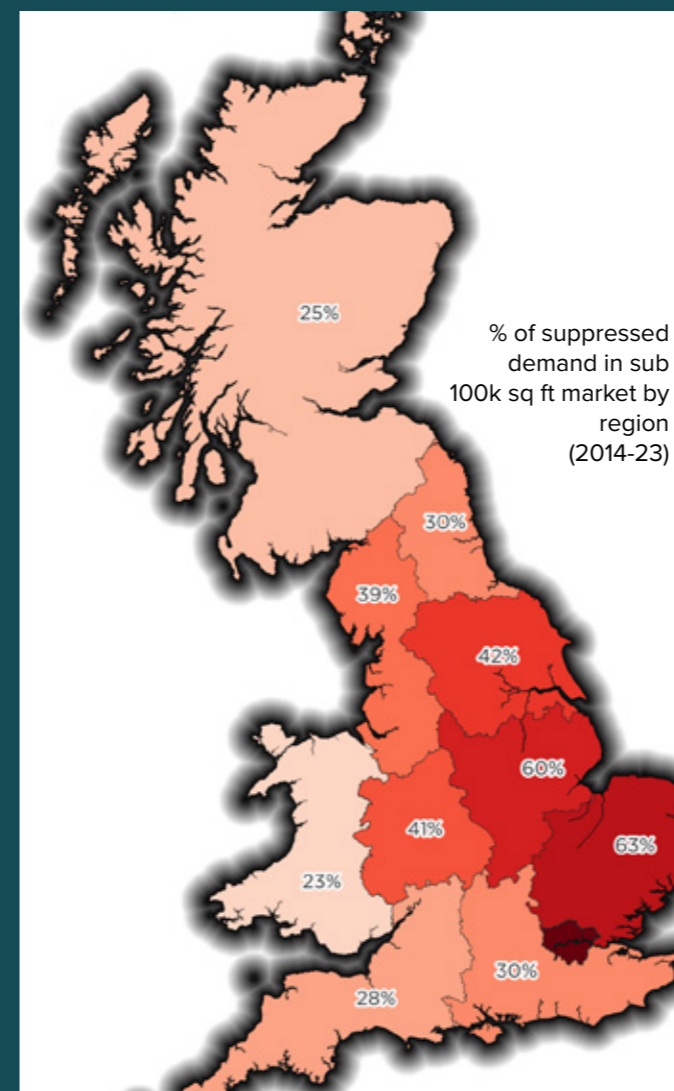
Figure 5.2 Sub 100k sq ft market availability rate vs. equilibrium (2014-24 YTD)



Suppressed Demand in the Small to Mid-box I&L Sector

Potter Space estimates that between 2014 and 2023, a staggering 63 million sq. ft of demand – approximately 38% – was suppressed in England within the sub-100k sq. ft market alone. Some areas such as the East Midlands is actually much higher.

Figure 5.3 Demand for sub 100k sq ft floorspace has been suppressed across all regions over the last decade



The lack of supply into the sub 100k sq ft market results in businesses not being able to find the space they need to grow. Instead, they have to “make do” with the space they occupy, effectively suppressing demand.

All regions across the UK had suppressed demand for I&L floorspace under 100k sq ft. On average the level of suppressed demand is 38% across the country, with areas such as the East Midlands and the East of England seeing suppressed demand equate to over 60%. London is very difficult to quantify given several different land uses compete for limited available stock but it’s likely to be higher than the East Midlands and East of England (figure 5.3).

This suppressed demand represents a missed opportunity for the UK economy, as if this floorspace were developed, it would provide further employment opportunities, help to limit the rampant rental growth and provide higher quality premises for smaller firms in order to boost productivity.

Addressing this shortage requires a concerted effort from developers, investors, and policymakers to recognise the vital role of small to mid-box units in the broader economic ecosystem. By rebalancing the focus towards this underserved segment, the UK can unlock new avenues for business growth, enhance economic resilience, and create a more dynamic and responsive I&L sector capable of meeting the diverse needs of businesses across the spectrum.

The Benefits of Unlocking Suppressed Demand

The Power of Unleashing Suppressed Demand

The immediate benefits to SMEs of increased sub-100k supply are clear, but it's important to note that this would also have a significant impact on the wider economy. In fact, Potter Space and Savills data reveals that supplying 63m sq ft of sub-100k premises could support the creation of 94,000 jobs. It could also directly and indirectly contribute £5.9bn GVA to the UK economy.

There are three areas that require collaboration and intervention to foster economic growth, support business growth journeys and enhance UK productivity.

If suppressed demand was realised, this could have resulted in:

- Potential on-site jobs: **Up to 94,000**
- Gross value added (direct): **£3.2 billion per annum**
- Gross value added (indirect): **£2.7 billion per annum**



Sufficient Supply

A lack of affordable premises stifles SME growth and exacerbates regional inequalities. Holistic planning reforms are pivotal in addressing this issue. By revising planning guidance and adopting a market-facing approach to estimating future employment needs, we can increase the supply of employment land.

This would ease the current affordability crisis, particularly acute for SMEs occupying sub-100,000 sq ft units. Implementing a 5-year employment land supply requirement, similar to housing, would empower councils to support new premises development.



Quality Premises with Good ESG Credentials

Modern, flexible premises that meet high ESG standards are essential for attracting skilled workers and reducing brain drain to London. Quality spaces enable the co-location of various business functions, enhancing operational efficiency.

Buildings with strong ESG credentials not only promote sustainability but also reduce operating costs. However, the industry faces an enormous challenge in the coming years as more stringent energy efficiency standards come into place, potentially rendering a majority of existing stock unlettable. Government support is needed to help landlords and occupiers meet these much-needed deadlines.



Premises in the Right Locations

The diverse locational requirements of sub-100k sq ft occupiers necessitate a nuanced approach to development. While some require direct access to strategic road networks, others need proximity to skilled labour pools and public transport.

Facilitating development in optimal locations improves supply chain efficiency, reduces transport costs, and ensures access to the right talent and customer base. We also propose a colocation approach that requires developers creating big-box schemes to assign a portion of the land for small to mid-box facilities.

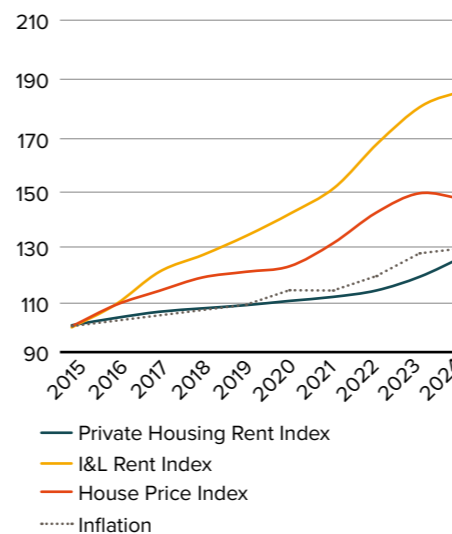
The Affordability Crisis

The UK has recently faced a period of inflation unprecedented in living memory, with operating costs soaring well above inflation rates, particularly in the last two years. This surge in expenses is placing immense pressure on businesses, threatening their viability and potentially impacting the broader UK economy.

Whilst acknowledging that rising rents make new developments viable the industry needs to consider the balance that allows both new developments to come forward whilst not constraining business investment. Rents, rates, fuel, electricity and labour costs are all rising significantly above inflation in recent years, creating a cost crisis for the SMEs that occupy small to mid-box premises (figures 6.1, 6.2, 6.3).

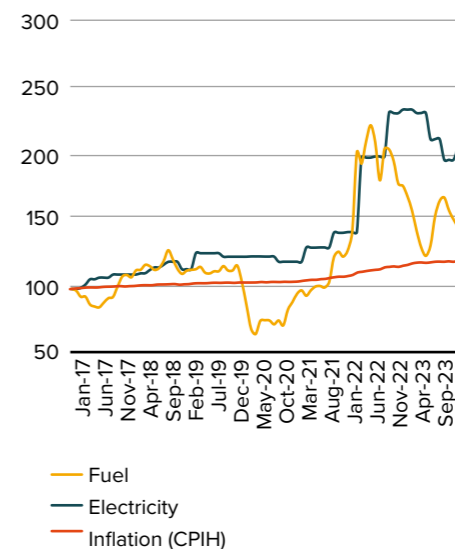
I&L rental growth has outpaced growth in house prices and private housing rents

Figure 6.1 I&L rental growth vs. housing rental and price growth and inflation (2015-24)



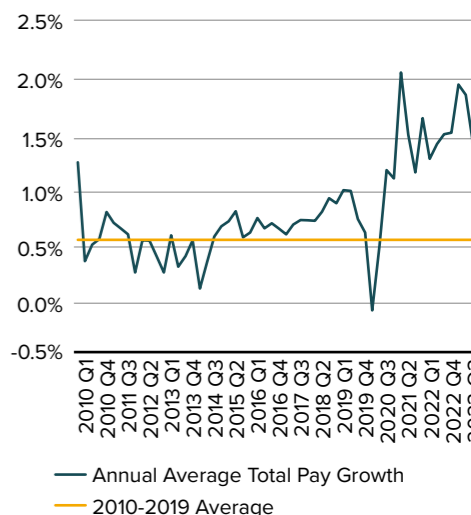
Fuel and electricity costs have been two of the main drivers of inflation in recent years

Figure 6.2 Fuel and electricity cost growth vs. inflation (2017-2024)



Labour costs have been growing faster than the long-term average in recent years

Figure 6.3 Annual wage growth vs. historic average (2010-19)



Global Supply Chain Pressures

Adding to these domestic pressures, global shipping costs have skyrocketed, with a staggering 115% increase since July 2023, as of October 2024. This spike is largely due to geopolitical tensions in the Red Sea and strained US-China trade relations, further squeezing SMEs who rely heavily on international supply chains.

A Unique Challenge

While factors such as shipping costs, fuel and electricity prices, and wage growth are influenced by broader macroeconomic forces, rental growth stands out as a variable directly linked to the supply-demand dynamics within the sector (figure 6.1). With warehouse demand recently outstripping supply market rents have for new premises have risen accordingly. We have started to observe a decline in take-up which suggests that many occupiers are choosing to remain in their existing units, rather than trade up into newer, more energy efficient properties. Without decisive action to increase supply of smaller units the market risks creating conditions that do not allow companies to grow into the big box occupiers of the future.

With costs continuing to rise for companies active in the I&L space there is a significant threat to individual businesses and the UK economy as a whole. The combination of rising energy costs, wages, rents, and global supply chain disruptions has created an environment which has seen company insolvency rise dramatically for companies in the retail, manufacturing and transport sectors.

The Regional Imbalance

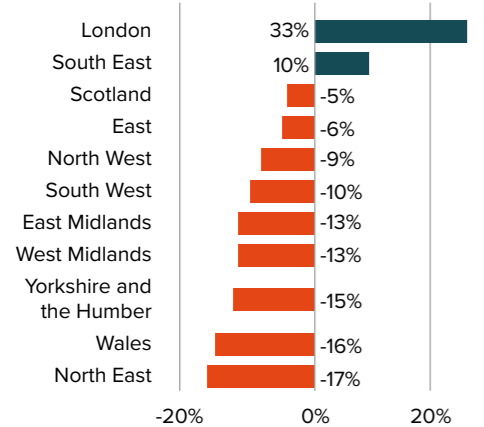
The Challenge

Regional economic output is severely imbalanced across the regions, with only London and the South East producing above the national average (figure 7.1). In other words, these two regions are driving a significant portion of the UK's total economy. A key reason for this is a lack of investment into other regions, particularly in R&D. Figures 7.2 and 7.3 show that these regions enjoy concentrated levels of R&D investment as well as higher wages than other regions.

Rebalancing this and moving away from a London-centric approach to investment and development is a key part of the levelling up agenda. But what role can I&L play in this?

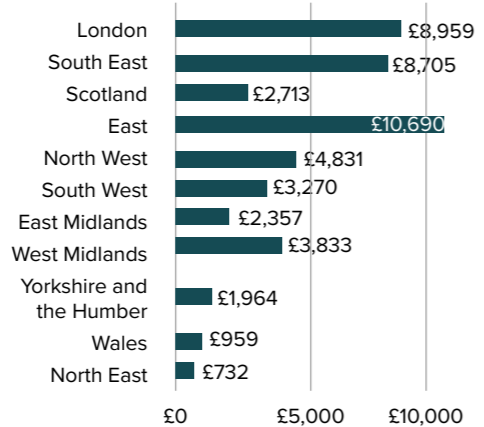
London and the South East are the only regions more productive than the national average

Figure 7.1 Regional output per hour relative to the UK average



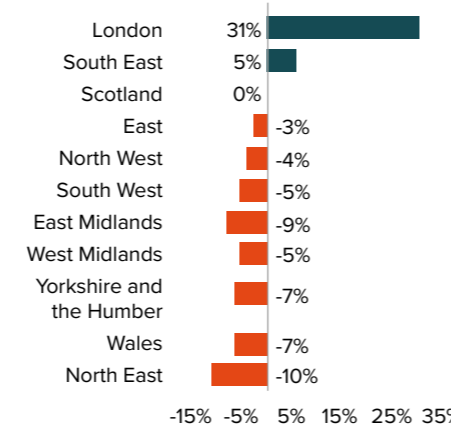
R&D spending is more concentrated in London, the South East and the East of England

Figure 7.2 Regional expenditure on R&D in 2022 (million)



London and the South East have higher pay levels than the national average

Figure 7.3 Regional average wages relative to the UK 10 average



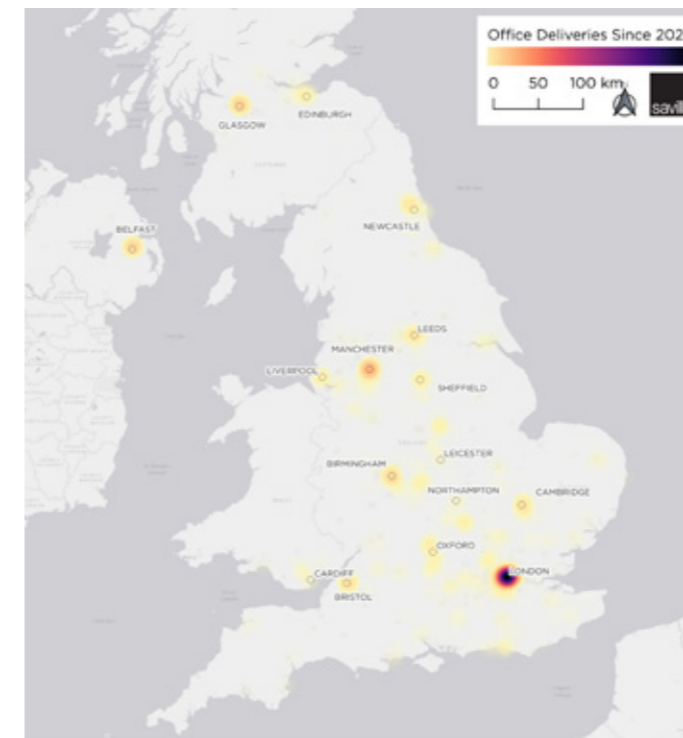
The Solution - Investing in the I&L Sector Helps to Rebalance the Regional Economy

Investment in supporting the I&L sector with the space needed to support growth, not only helps to realise significant economic benefits currently being suppressed, but it will also help to rebalance the regional economy. By way of comparison, figure 8.1 below highlights the geographical spread of office developments since 2020 in comparison to the geographic diversity or the delivery of new stock into the I&L market over the same period in figure 8.2.

Delivering high quality, sustainable business premises in a variety of settings – town centres, business parks, along transport networks – creates local jobs and boosts economic output on a long term basis. The flexibility of smaller premises which can be adapted to business needs relatively easily, and the high levels of demand for such premises, mean occupation levels are likely to remain high and the local economy will become more resilient and adaptable to wider conditions.

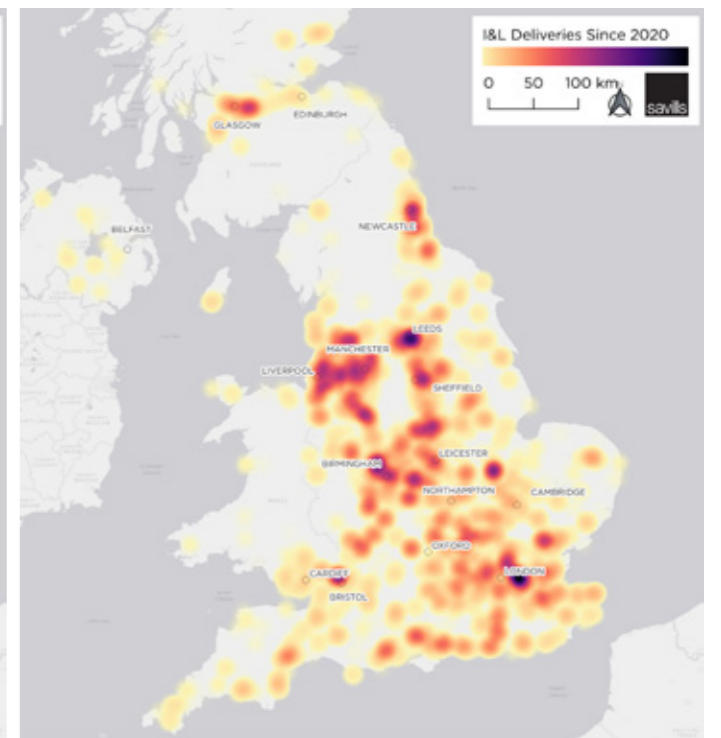
Office development is concentrated in major cities

Figure 8.1 Location of office development since 2020



I&L development is much more geographically diverse

Figure 8.2 Location of I&L development since 2020



Innovation Challenges in the UK from Start-up to Scale-up

A picture of unrealised potential

The UK stands as a beacon of innovation on the global stage, boasting a thriving start-up ecosystem that rivals the world's best. Since 2020, the UK has consistently ranked second only to the United States on the Global Start-up Ecosystem Index, with London matching New York's performance as a start-up hub, and trailing just behind Silicon Valley.

However, the complex reality means that the UK's innovative potential often struggles to translate into long-term growth and productivity. By delving into the paradox of the UK's strong start-up culture and its challenges in scaling businesses and commercialising research, Potter Space addresses what can be done to help.



A World-Class Start-up Ecosystem with Scale-up Struggles

The UK's start-up scene buzzes with energy and potential, attracting talent and investment from across the globe. Yet, beneath this surface lies a concerning trend. In 2022, the UK witnessed a troubling shift as the rate of company closures surpassed new registrations, resulting in a net loss of businesses (see figure 9.1).

This stark reality contrasts sharply with the European landscape, where over the past decade, company birth rates have consistently outpaced closures by more than 2%. This high mortality rate among UK businesses signifies a critical failure to fully capitalise on the nation's world-class educational institutions, innovative spirit, and research capabilities.

The UK, ranking 4th in the Global Innovation Index with strengths in research and development, finds itself grappling with the challenge of transforming its intellectual and creative outputs into tangible, market-ready products and sustainable businesses. The gap between the most and least productive firms in the UK is widening, suggesting the less productive firms need support (figure 9.2).

The Innovation Paradox: Research Without Development

At the heart of this challenge lies what can be termed the UK's 'innovation paradox'. While the country excels in producing cutting-edge research and fostering a culture of innovation, it struggles to bridge the gap between academic breakthroughs and commercial success. The European Innovation Scoreboard highlights this disparity, pointing out the UK's weakness in translating innovations into marketable products and services.

This disconnect manifests as a form of 'research without development', where world-leading discoveries and innovations often fail to make the crucial leap from laboratory to marketplace. The lack of space to scale and mass-produce these innovations contributes to the UK's ongoing productivity challenges.

The repercussions of this gap between innovation and commercialisation extend beyond the immediate loss of potential products and services. It impacts the broader economy, constraining productivity growth and limiting the UK's ability to fully leverage its intellectual capital in the global marketplace.

The conclusion that can be taken from this data is that the UK's innovation landscape presents a picture of unrealised potential. The nation's ability to foster a world-class start-up ecosystem and produce groundbreaking research is undeniable. However, the struggle to transform these assets into sustainable businesses and marketable products represents a significant economic bottleneck.

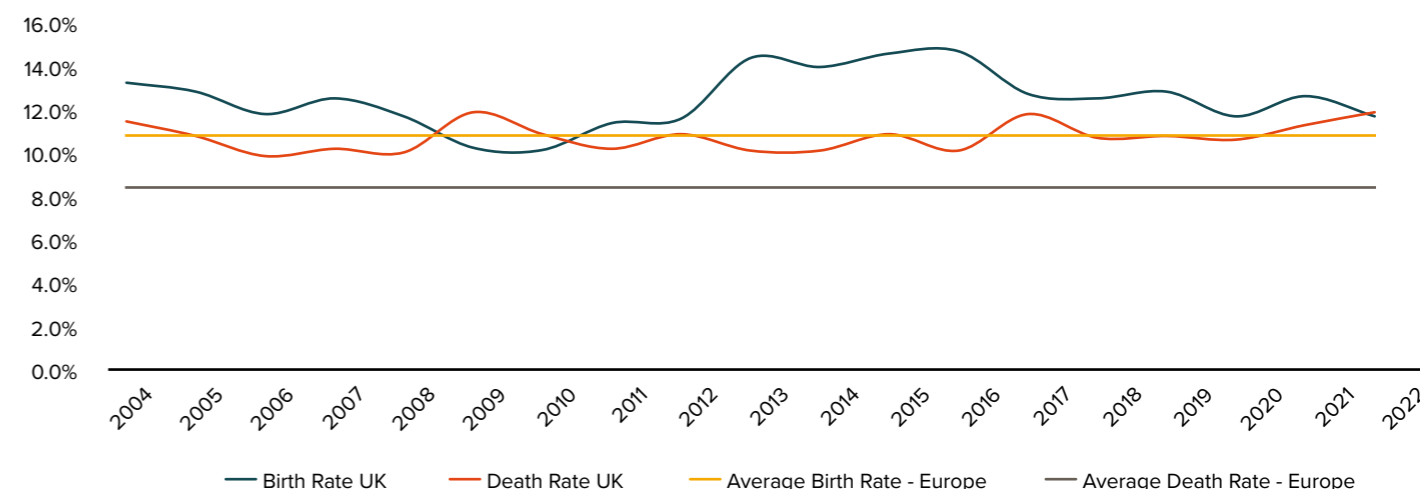
Addressing this challenge requires a multifaceted approach. Targeted support to guide businesses through the crucial scale-up phase, stronger links between research institutions and industry, and policies that encourage the commercialisation of innovations will all be required.

By bridging the gap between its innovative prowess and commercial success, the UK can unlock new avenues for economic growth, enhance its global competitiveness, and fully realise its potential as a leader in the rapidly evolving technological landscape.

The path forward lies in nurturing not just the birth of new ideas and businesses, but in cultivating an environment where these innovations can grow, thrive, and make a lasting impact on the UK's economic prosperity. Suitable property and facilities are a key part of this.

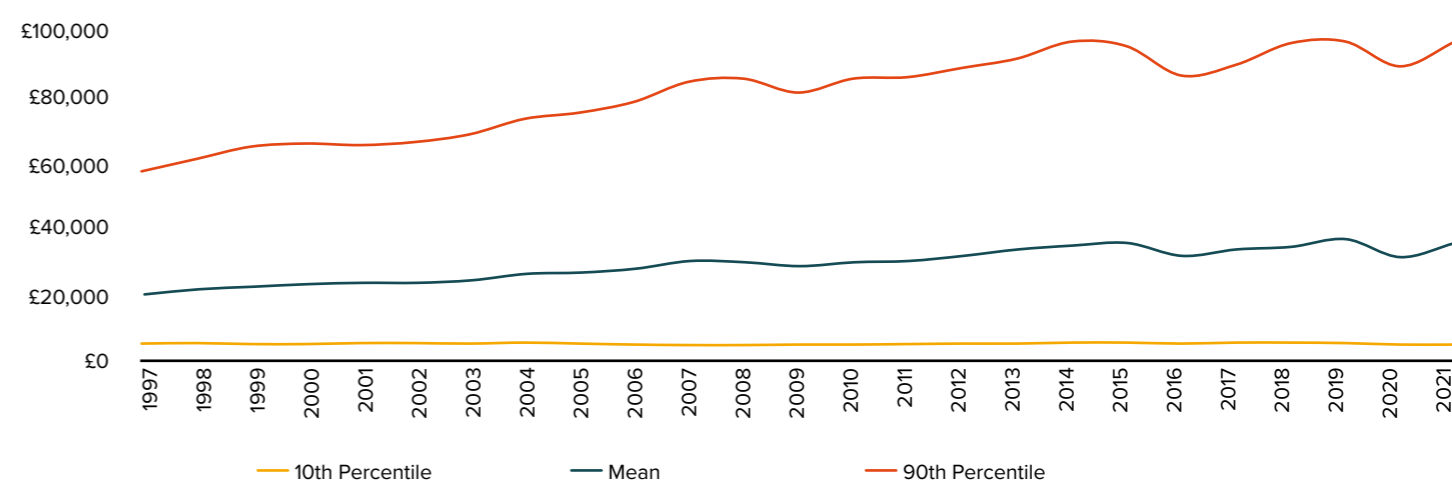
The UK has a higher birth and death rate of firms compared to Europe

Figure 9.1 Birth and death rate of UK firms vs Europe



The gap between the UK's most and least productive firms has widened since 2008

Figure 9.2 GVA per worker - 10th vs 90th percentile of UK firms



The EPC Cliff Edge

As the sector grapples with supply shortages, a new challenge looms on the horizon: meeting future minimum energy efficiency standards. This issue is particularly acute in the small to mid-box market where a significant portion of existing premises are falling short of upcoming requirements (**figure 10**).

While retrofitting has been proposed as a solution, it presents its own set of complications and may not be sufficient to address the problem comprehensively.

Current State and Future Requirements

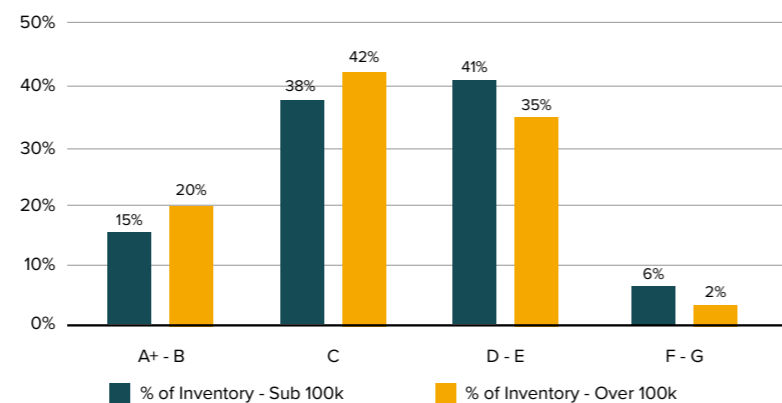
Within the sub-100k sq ft category, a staggering 47% of inventory currently holds an EPC rating below C. Whilst this figure is 10% worse than the 37% of unfit stock in the bigbox market, this issue is clearly an industry wide problem.

The poor EPC ratings within the small to midbox market in particular is a result of the historical lack of investment in smaller units, compounded by rising rents that force many companies to remain in older, less efficient premises.

Without any interventions, this situation is unlikely to improve in time for the expected EPC thresholds coming into force.

I&L units under 100k sq ft are of worse quality than units over 100k sq ft on average

Figure 10 % of I&L units under 100k sq ft by EPC ratings



The implications of these standards are profound. Without significant upgrades, 6% of current sub-100k sq ft inventory is already unlettable.

By April 2027, this figure is projected to skyrocket to 47%, and by 2030, an alarming 85% of existing inventory could be rendered unlettable under the new regulations.

The government's Minimum Energy Efficiency Standards (MEES) are expected to set increasingly stringent requirements:

- Since 1st April 2023, commercial properties must achieve at least an EPC rating of E to be let.
- If proposed reforms are adopted, from 1st April 2027, this requirement will rise to a minimum EPC rating of C.
- By 2030, the bar is set to rise further, mandating a minimum EPC rating of B for all lettable commercial properties.

The Retrofitting Dilemma

In response to this looming crisis, institutions such as the UK Green Building Council (UKGBC) and numerous local authorities have advocated for retrofitting existing poor-quality stock. While this approach is crucial for fostering a green and thriving economy, it is not without its challenges.

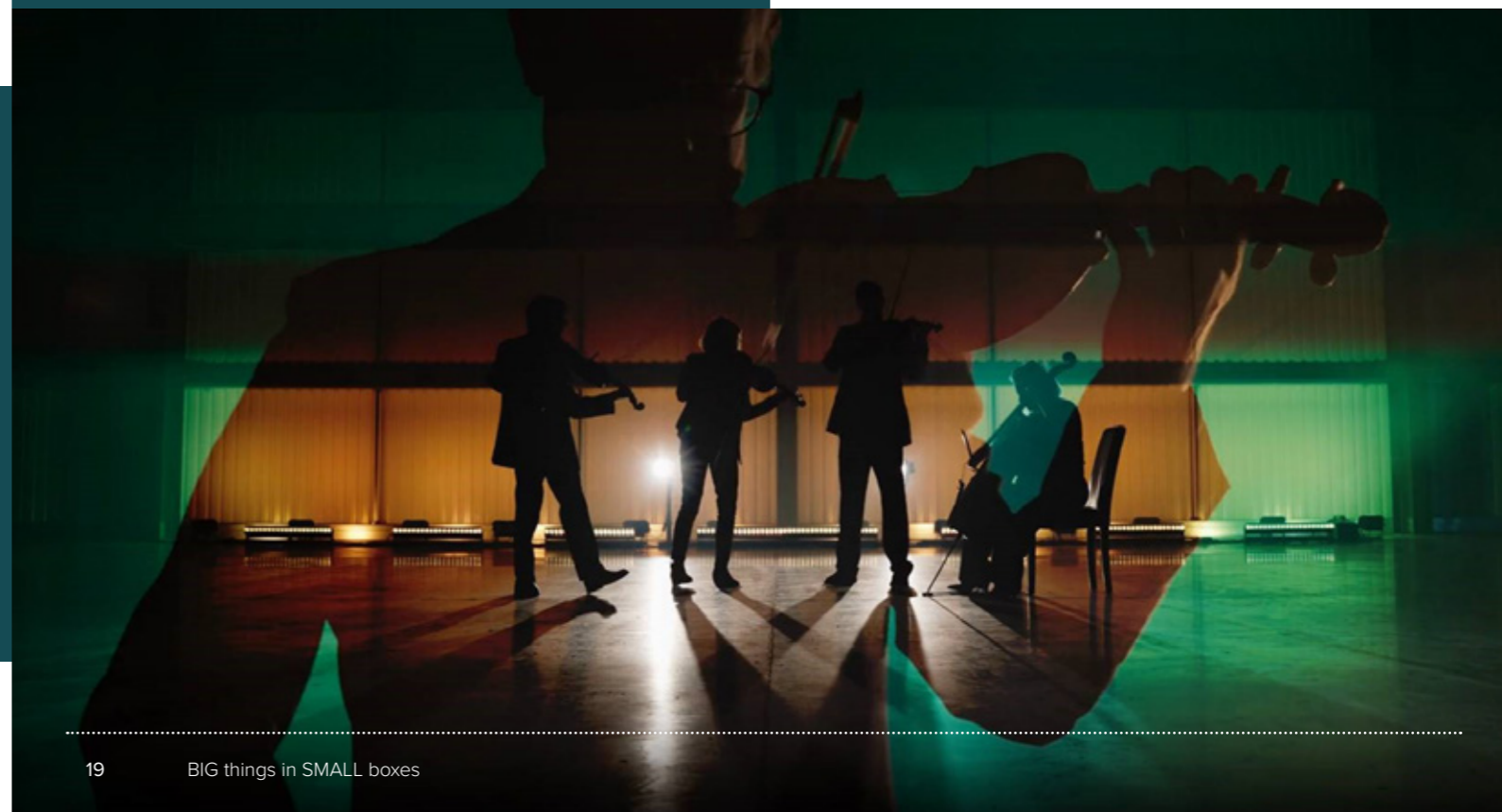
Retrofitting presents several significant hurdles:

- 1. Tenant Displacement:** The process typically requires vacant possession, thereby terminating leases at expiry, causing disruption to businesses and a loss of rental income for property owners.
- 2. Supply Chain Pressure:** Given the existing supply shortage, displaced tenants may struggle to find alternative economic premises, potentially forcing some to cease operations entirely.
- 3. Exacerbation of Supply Issues:** Large-scale retrofitting could further tighten the already constrained supply of affordable lettable space, particularly impacting smaller occupiers.
- 4. Limited Scope:** While retrofitting can upgrade existing stock, it cannot address the demonstrated demand for new, high-quality floorspace in the market.
- 5. Feasibility:** Many premises are in such a condition or compromised configuration that retrofitting is impractical, requiring a full rebuild, or prohibitively expensive, meaning the property is most likely to fall out of use or be repurposed.

The energy efficiency challenge facing the small to mid-box I&L sector requires a nuanced approach. While retrofitting is an essential component of the solution, it alone cannot address the full scope of the problem. The sector must balance the need for energy-efficient premises with the pressing demand for additional space and the practical realities of upgrading existing stock.

Addressing this challenge will require a coordinated effort from property owners, tenants, policymakers, and industry bodies. Innovative solutions that minimise disruption to businesses, strategic investments in new energy-efficient developments, and flexible policy approaches may all be necessary to navigate this complex landscape.

As the deadlines for stricter energy efficiency standards approach, the I&L sector, particularly in the small to mid-box market, faces a critical juncture. The decisions and actions taken in the coming years will not only shape the sustainability of the sector but also its capacity to support the broader UK economy in an increasingly environmentally conscious business landscape.



Sustainable Energy Potential

The sub 100k I&L sector has the potential to deliver up to 11.6 TWh of energy from rooftop solar, enough to power over 4.3 million homes.

- Power availability has become a key concern for many stakeholders within the I&L sector.
- On top of the current power requirements, the I&L sector is experiencing a technology overhaul. New technology such as robotics, automated stacking systems and electric vehicles will increase power requirements into the future.
- Alongside growing power requirements, there has also been a conscious push towards ESG and net zero from companies as they seek to decarbonise supply chains.
- The sub 100k I&L sector has the ability to provide sustainable power, through rooftop solar photovoltaic (PV) panels. Analysis by the UK Warehousing Association (UKWA) demonstrated the potential of warehouses over 100k sq ft to deliver rooftop solar PV panels, but there is also the potential to deliver panels on units under 100k sq ft.
- There is over 201 million sqm of roof space on units under 100k sq ft in the UK, which has the ability to provide up to 11.6 TWh annually. This capacity is broadly equivalent to the solar capacity of the UK grid in 2023 and could be enough to power over 4.3 million homes.
- The rooftops of existing and future I&L buildings provide an efficient pathway to deliver solar power, which is especially important for meeting biodiversity and climate goals.



Case Study: Potter Space - Ripon

Potter Space's new units at Ripon Business Park benefit from the incorporation of solar panels on the rooftops. The power generated from these PV panels supports EV charging points, ancillary office floorspace and adoption of future technologies.

Solar capacity within I&L units under 100k sq ft



Floorspace

201 million sqm



Potential Generation p.a.

11.6 TWh



Can Power

4.3 million homes

Source: Savills I&L Future Space Report 2024, Savills power calculations



Conclusion

Unlocking the Potential of the Small to Mid-box I&L Sector

To harness the full potential of the small to mid-box I&L sector, a coordinated and strategic approach is essential.

This requires:

Planning Reform

Implementing holistic planning reforms, including revisions to national planning guidance, to facilitate sufficient supply of affordable premises and support economic growth.

We encourage policymakers to understand the economic potential in the data brought to light by Potter Space and play their part in facilitating growth and development. The planning reform needs to consider the following factors:

- **Balancing small, mid and big box:** Ensuring a good supply of a range of sizes of stock to meet the needs of the market.
- **Strategic location planning:** Facilitating development in optimal locations to improve supply chain efficiency, attract talent, and provide better access to customers and businesses. This will require further understanding of the locational requirements of businesses.
- **Policy support:** Crafting policies that recognise the unique challenges and potential of the small to mid-box sector, supporting its growth and sustainability for the good of the country as a whole, allowing the UK to once more compete economically on a global stage.
- **Timing:** The planning system is severely underfunded and under staffed leading to long delays for planning approvals. The government must find ways to accelerate planning approvals.

The Labour government's proposed planning reforms reflect a more positive approach to planning for future economic growth by supporting uses such as labs, gigafactories, data centres and freight and logistics which the government have now announced new legislation to accelerate delivery.

There is also recognition and enhanced support for the role that the I&L sector plays in supporting supply chains, transport innovation and decarbonisation.

The Grey Belt (defined as previously developed land that does not meet Green Belt purposes) is now a new source of land supply to meet housing and employment needs.

Restoring the 5-year housing land supply requirement is welcome, but this should also be extended to employment land so that Councils can better support the development of new premises.

Revisions to planning guidance will also be required if a sufficient supply of employment land is to be facilitated. This should involve a more market-facing approach to estimating future employment needs, such as Savills Suppressed Demand methodology which accounts for historic supply constraints.



Supporting Sustainable Stock

Re-appraising the EPC milestones to help achieve the governments goals to achieve carbon neutral targets. This would mean working closely with industry to understand the challenges the current targets present and the potential catastrophic impact on an already underserved market.

- **EPC deadlines:** Review of the deadlines for EPC adoption to ensure they are achievable whilst reducing the potential impact on the UK economy.
- **Investment in quality premises:** Encouraging development of high-quality, flexible spaces with strong ESG credentials to attract skilled workers and support business growth. I&L needs to cater to the changing needs of emerging industries in order to support the sector and the economy at large.
- **Energy efficiency solutions:** Developing innovative approaches to upgrading existing stock while simultaneously investing in new, energy-efficient developments. The EPC cliff edge is looming and currently the industry is taking a head in the sand approach to preparation. Small to mid-box properties are likely to be hardest hit for affordability reasons, and they require support.
- **Tax breaks or incentives:** If the government is intent on meeting the Net Zero deadlines, consideration should be given to tax breaks or incentives to help with this transition.

Industry Collaboration

Encouraging collaboration across the industry to explore more solutions to provide a range of spaces for business to use. These ventures could enable sharing of land and infrastructure to ensure the right stock is available.

- **Mixed schemes:** Encouraging developers to work together to create diverse estates which will meet the increasingly growing needs of the market.
- **Infrastructure & grid capacity:** The UK is suffering from capacity issues in relation to electrical grid supply. The grid needs improving to allow the Net Zero agenda to thrive.

The small to mid-box I&L sector is not just a component of the UK's economic infrastructure; it is a vital engine for growth, innovation, and regional development. By addressing its challenges and capitalising on its potential, we can unlock significant economic benefits, drive sustainable development, and create a more resilient and balanced UK economy.

At Potter Space we will continue to champion small to mid-box as a cornerstone of the UK's economic future, driving prosperity and sustainability for generations to come. We are actively developing available land into high quality, sustainable homes for businesses and aiming to be best in class at what we do.



About Potter Space

Home for Business

Potter Space is a property company specialising in the industrial and logistics sector. The company owns, develops, and operates high-quality industrial and logistics spaces in key locations across the UK. With five strategically located business parks, Potter Space encompasses over 1.7 million sq. ft of existing commercial space and 250 acres of land primed for strategic development. These parks boast excellent connectivity via road, rail, and potential waterways to key cities and ports.

As a family-owned company with a 60-year legacy, Potter Space has built enduring relationships with its customers, operating at near 100% occupancy with many long-standing partnerships. The company is home to diverse businesses spanning sectors such as manufacturing, e-commerce, and consumer products.

Potter Space believes that the sub-100k sq. ft, or small- to mid-box market, is an unsung hero within the Industrial & Logistics (I&L) sector. The company continues to invest in understanding and championing this area, recognising its importance to the UK economy.

Sustainability is at the forefront of Potter Space's development strategy. The company aims for a minimum BREEAM 'Excellent' accreditation on all future buildings, prioritising sustainability, biodiversity, health, and wellbeing across all its business parks.

To meet growing demand, Potter Space is currently developing across 250 acres. The company's business parks are in Ely, Selby, Ripon, Droitwich, and Knowsley, each managed by a team of industry experts who work in partnership with clients to support their strategic growth and ensure individual needs are met.



Savills Contributors

Mark Powney
Director, Economics

Kevin Mofid
Head of EMEA Industrial and Logistics Research

Reyna Nayee
Senior Economist, Economics

Callum Hodgson
Economist, Economics



Home for business