

Viability Study

**265 Burlington Road,
New Malden, KT3 4NH**

By

Turner Morum LLP

Private & Confidential

July 2019

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1. BACKGROUND AND RELEVANT EXPERIENCE

- 1.1. My name is Nicholas Bignall of 32-33 Cowcross Street, London EC1M 6DF. I am a Member of the Royal Institution of Chartered Surveyors ("RICS") having qualified in 2013 following the award, in 2009, of an Honours Degree in Land Management from University of Reading and in 2010 a Master's Degree in Urban Planning & Development.
- 1.2. In 2010 I joined the practice of Turner Morum Chartered Surveyors and was made an Associate in 2015 and a Partner in 2018. I am a specialist in the field of development site appraisals and associated subjects.
- 1.3. I regularly advise across the whole of the UK on the value and potential of major tracts of development land and infill urban development focusing specifically on development sites within the London Boroughs. I am currently instructed by a number of Local Authorities, Landowners, Housing Associations and Developers and have extensive experience in this field. Full details of some of my recent case experience can be viewed at **Appendix 7**.
- 1.4. Turner Morum were appointed by Mr. Jonathan Murch on behalf of Redrow Homes ('the applicant') in November 2018 to undertake a viability assessment in regards to their proposed development at 265 Burlington Road, New Malden. The scheme is for 456 residential units (flats) equating to a Gross Internal Area (GIA) of some c. 513,000 square feet. The development is described as follows:-

"Demolition of the existing buildings and erection of two blocks of development ranging in height between seven and 15 storeys and comprising 456 new homes, of which 114 will be one beds, 290 will be two beds and 52 will be three beds. 499sqm of B1(a) office space will be accommodated at ground floor level along with 220 car parking spaces, 830 cycle parking spaces, a realigned junction onto Burlington Road, hard and soft landscaping and associated residential facilities. The application also includes minor changes to the layout and configuration of the retained Tesco car park."

- 1.5. The subject site is located in the London Borough of Merton and is on the north side of Burlington Road. The site is currently separated into two uses; 265 Burlington Road which is a two storey industrial and office building and the car park annexe to the Tesco supermarket. A location plan can be viewed as per **Appendix 1**.
- 1.6. I have carried out a development appraisal adopting a bespoke valuation model structure to analyse the viability of the proposed scheme. The residual appraisals and supporting information can be seen as **Appendix 2**.
- 1.7. In undertaking this viability analysis I can confirm that my approach and methodology accord with the Mayoral Supplementary Planning Guidance *Homes for Londoners August 2017 (SPG)*. Furthermore, in undertaking the viability I am aware and follow other supporting viability guidance documents as the RICS *Financial Viability in Planning and Viability Testing Local Plans* (the Harman report). I am also aware of the Planning Practice Guidance on Viability published following updates to the National Planning Policy Framework (NPPF).

2. MECHANICS OF THE ASSESSMENT

2.1. My residual appraisal analysis can be summarised as follows:-

- **Appendix 2 Tab 1A** – Appraisal showing the viability of the proposed scheme with **35%** affordable housing on a habitable rooms basis (145 units) with a 68/32 split as affordable rent/shared ownership.
- **Appendix 2 Tab 1B** – Appraisal showing the viability of the proposed scheme with **11%** affordable housing on a habitable rooms basis (45 units) with a 65/35 split as affordable rent/shared ownership.

2.2. I will now run through the various appraisal inputs in sequential order as they appear in my residual appraisal analysis:

REVENUES

- 2.3. Market revenues for the residential units are based upon a pricing schedule provided by Redrow based upon research of comparable sites in the locality. Estimated values range from £354k to £669k at an average rate of c. **£675** per square foot as per **Appendix 3**.
- 2.4. To support this pricing schedule I have reviewed a number of comparables which are also included as **Appendix 3**. One can observe within this schedule that the average price of comparables reviewed equates to c. £673 psf, which supports the pricing schedule I have been provided with. Within this I have highlighted the One New Malden development which I believe is the best direct comparable for this scheme. This site shares similarly sized 1, 2 and 3 bed units to our scheme and is located less than a mile away.
- 2.5. From the evidence I have been able to source I have outlined the following most recent 2019 marketing prices at One New Malden which indicate the assumed achieved sales value in my appraisal are reasonable:
- **1 BED**
 - £380,000 – 538 ft² - **£706 psf**
 - £375,000 – 538 ft² - **£697 psf**

 - **2 BED**
 - £497,500 – 797 ft² - **£624 psf**
 - £465,000 – 759 ft² - **£612 psf**

 - **3 BED**
 - £695,000 – 1,138 ft² - **£610 psf**
 - £580,000 – 1,050 ft² - **£552 psf**

- 2.6. The above market revenue evidence needs to also be considered in the context of the prevailing housing market in London. This is confirmed in the latest RICS Residential Market Survey April 2019 (**Appendix 5**) which reports that **“the regional breakdown again shows prices under pressure particularly in London and the South East, while the South West has now consistently returned negative readings on this measure for the past six months”**.
- 2.7. Affordable values have been benchmarked at 65% of OMV for shared ownership whilst the affordable rent values have been calculated in accordance with the weekly rent levels outlined as per the GLA London Affordable Rents 2019/20. I would suggest the above allowances are considered as fairly standard industry positions.
- 2.8. To support the position on shared ownership I have cross referenced using a Discounted Cashflow Analysis. The basic premise of the DCF model is to take the full market value of the units and discount them over an assumed 30-year staircasing period. A capital receipt is then calculated for each tranche payment, based on the discounted Market Value figure for the year in which it falls, whilst accounting also for the rent paid on the retained share of the property, and any associated costs. This produces a yearly income total, the sum of which produces a gross revenue figure, from which one would then deduct appropriate costs and marketing fees etc.
- 2.9. For a DCF the standard assumptions include 4 x 25% tranche payments (including initial deposit) in Years 1, 10, 20 and 30. Over this 30 year stair casing period whereby purchasers will step up to 100% equity with a corresponding reduction in rents over the period – this is then capitalised with a discount rate of 6.5% taking account of anticipated management costs, allowance for bad debts and inflation (1.5%). I have also assumed a rent charge of 2.0% on the retained portion of the unit. This produces a value of c. £435 which supports the 65% allowance adopted in my appraisal and is in line with my £ psf allowance.

2.10. Ground rents are included at a rate of £10 p.a. for each private dwelling capitalised at a 5.5% yield. The income is capped at this level in line with the latest Government consultation on leaseholder reforms.

DEVELOPMENT COSTS

2.11. Fees and marketing costs in respect of the development are included at 3.0% of Market Housing Gross Development Value ("GDV"), and the cost of disposing of the affordable units to a Registered Provider is included at 0.5% of affordable GDV, as per standard industry benchmarks.

2.12. The construction costs associated with this scheme are included based upon an independent cost plan provided by Mr. Jon Marriot of Ward Williams Associates (WWA) who are specialist cost consultants – the full details of their cost plan can be viewed as per **Appendix 4**. For the purpose of this exercise I have included the total build cost in my appraisal at c. **£255 psf** equating to c. £130.5m.

2.13. An allowance for Technical Fees is included at just 6% of the Standard Build Cost which reflects the costs associated with Architects, Quantity Surveyors, Engineers, Project Management and other technical / professional consultancy fees. By way of comparison, the suggested allowance for professional fees within the 3 Dragons model is 12% of standard build costs and I would therefore contend that the 6% adopted in my appraisal should be considered as conservative.

2.14. I have then made an allowance for Developer Profit at 20% (of GDV) for the Market Housing and 6% (of GDV) for the affordable housing. I would suggest these assumed returns are within industry accepted industry parameters and the above allowances result in a blended return of 17.1% on GDV in the 35% appraisal model (**Tab 1A**).

2.15. Arguably a development could be considered unlikely to come to fruition unless it can achieve a profit margin of around 20% of GDV (blended). Banks require

Developers to illustrate these levels of developer profit before they will provide development finance and clearly such is considerably higher than that shown in my analysis.

- 2.16. I believe this to be all the more pertinent following the Brexit referendum vote and the subsequent triggering of Article 50. The uncertainty which envelopes these negotiations has fed through into the economy and particularly the housebuilding industry (see **Appendix 5**); I believe it to be widely acknowledged that the current climate is one of rising costs and stalling revenues and as such in these times it is all the more important for developers to maintain sufficient target profit margins to ensure they are compensated for the level of risk involved.
- 2.17. Section 106 (S106) has been included at an estimated £1.5m in both tested scenarios. Should further information regarding S106 contributions be forthcoming I would need to update my assessment accordingly.
- 2.18. CIL has been included based upon calculations within each of the two scenarios (see Tab 4). This adopts the market housing floor area (in square metres) in each case and applies a general residential net to gross of 80% (based upon an approximate average from the schedule of accommodation). For the Mayoral CIL calculation, I have also included the floor area of the commercial space (499 square metres), and to both CIL rates I have then applied the appropriate indexation using BCIS All-In TPI. The results are total CIL figures ranging from circa £5.88m (within the 35% affordable scenario) to circa £8.07m (within the 'break even' 11% affordable scenario).
- 2.19. With regards to the calculation of finance, I have included within my appraisal a quarterly cashflow to reflect the cost of finance for my appraisal analysis. This can be seen as per **Tabs 5A – 5B of Appendix 2** and reflect the details of the particular scheme including the build rate of the residential units and the particular build cost timings.

2.20. I have made the assumption that construction will commence on site within Q1 Year 1 (this is assumed to be a period of site preparation) and will be completed by the start of Q2 Year 3. I have also assumed a significant proportion of the units will be sold 'off-plan' with the remainder of the residential units being disposed of post-completion at a rate of 30 market completions per quarter. I have assumed a finance rate on debit of 6.50% which I believe is reasonable in the current climate.

3. VALUATION METHODOLOGY

- 3.1. The issue of what is deemed to be an appropriate Land Value for inclusion within viability studies is at present a highly topical subject. Planning appeal decisions and government guidance dictate that one has to ignore the amount that is actually paid for a development site and instead adopt an appropriate Existing, Alternative or Benchmark Land Value.
- 3.2. The Structure of my Residual Appraisals produces a Residual Land Value (RLV) which is then compared with the Existing or Alternative Use Value (EUV/AUV). If the RLV exceeds the EUV/AUV, a surplus is generated and the scheme can be deemed "Viable". However if the RLV is less than the EUV/AUV, a deficit is produced and the scheme should be considered "Non-Viable".
- 3.3. In this case I have included the land value on the basis of the site's Existing Use Value (EUV) based upon an independent report provided by Mr. Alex Reade MRICS who is an Associate Director at GL Hearn (see **Appendix 6**). One can observe from his report he has estimated the existing freehold value of the site to be **£5.98m**. Full details of how Mr. Reade has arrived at this figure can be viewed as per **Appendix 6** however, in summary, the total EUV is split as c. £4.5m value for the office space at 265 Burlington Road and £1.48m for the car parking area.
- 3.4. This approach to assessing the sites Benchmark is recommended in various pieces of viability guidance including the Mayor's "*Homes for Londoners*

Affordable Housing and Viability Supplementary Planning Guidance” (SPG) (August 2017).

- 3.5. Although I have adopted a land value based on the site's EUV, I have also considered the Alternative Use Value (AUV) of the subject site. I understand that there is no obvious reason why permission wouldn't be granted for a change of use from the existing office use to residential under permitted development (PD) rights. I have been provided with an accommodation schedule for a hypothetical PD scheme from TP Bennett LLP (architects on the project) including 36 apartments containing a mix of 1, 2 and 3 bed units.
- 3.6. I have inputted this schedule into a residual appraisal which can be viewed in detail as per **Tab 6 Appendix 2**. As one can observe from this appraisal I have maintained the same assumptions as with the proposed scheme appraisal for inputs such as revenues, marketing, fees and profit. For the build costs I have liaised with Mr Mark Stevens of WWA who advised that a recent PD project he worked on in Maidenhead was costed at c. £125 - £130 psf. For this exercise I have assumed a PD build cost of £140 psf.
- 3.7. The result of this analysis is to produce an AUV for the subject site of **£6.203m** which is higher than the £5.98 EUV adopted within my assessment.

4. SUMMARY CONCLUSION

- 4.1. The outturn of my analysis can be summarised as follows:

Tab	Description	Residual Land Value	EUV	Surplus / Deficit	Viable/ Non-Viable?
1A	35% Affordable	-£8,101,696	£5,980,000	-£14,081,696	NON-VIABLE
1B	11% Affordable	£6,049,723	£5,980,000	£69,723	VIABLE

5. CONCLUSIONS

- 5.1. It will be clear from the above table that the scheme demonstrates a deficit of c. **-£14.082m** at **35%** Affordable Housing and can therefore be considered to be technically non-viable. The sensitivity scenario 1B shows that the level of affordable housing would need to reduce to **11%** affordable in order for the scheme to become 'break even' and be considered viable.
- 5.2. In my experience, where certain deficits are incurred in viability the developer can sometimes chose to take the 'commercial decision' to proceed with a scheme at a certain level of affordable housing, provided that the deficit does not increase any further. This 'commercial decision' would be reached on an individual site basis and formed on the assumptions within this appraisal.
- 5.3. On this basis the applicant has advised me that they are prepared to deliver the scheme as per the (Scenario 1A) appraisal in my submission with a provision of **35% affordable housing**. This is clearly significantly in excess of the 'break even' position of 11% affordable housing which represents the maximum reasonable percentage of affordable housing achievable from the proposed development.
- 5.4. I hope this provides a sufficient level of information. I would welcome the opportunity to discuss the findings of my analysis with you at your earliest convenience.

Turner Morum LLP

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