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Mr E Durrant
Principal Planning Officer
South Cambridgeshire Hall
Cambourne Business Park
Cambourne
Cambridge CB23 6EA

Dear Ed

CAMBOURNE WEST – VIABILITY ASSESSMENT, INDEPENDENT REVIEW

1. Executive Summary

1.1 We have reviewed the updated report by Turner Morum (TM) dated 29 June 2016 and concluded that the main issues relating to the viability of the scheme are the base build cost, abnormal costs and infrastructure costs, in so far as these costs are high and front loaded which has a negative effect on the scheme's viability.

1.2 We have reviewed the inputs and assumptions used by Turner Morum as set out below and found them on the whole to be reasonable, with the exception of

i) The value of the shared ownership units
ii) The value of the affordable rented units
iii) The base build cost
iv) The abnormal and infrastructure costs relating to the scheme

1.3 The applicant's appraisal shows (with an affordable housing offer of 30% by unit and S.106 contributions of £61.02M) a residual land value of XXXX which equates to XXXX/gross acre.

1.4 The benchmark land value for the subject site, as set out in my report of February 2016 is appropriate at XXXXXXX or XXXX in total. It can therefore be seen that the scheme is unviable to deliver the level of affordable housing at 30% of units which has been offered.

1.5 I have been provided with an independent appraisal, carried out by Mr Ousby of the Council, and whilst I have not been instructed to check the veracity of that appraisal, it shows an even lower residual land value at XXXXXXXX in total. Thus, taking this figure build costs would have to reduce significantly or sales values improve significantly to make the 30% offer work.

1.6 From the correspondence I have been provided I can see that the applicant is proposing that they deliver the 30% affordable housing without a viability review mechanism per phase. Whilst it is normal for the Council to seek such a review mechanism, because the scheme is failing to deliver 40% affordable housing, the initial deficit noted above, combined with the high upfront infrastructure costs lead me to conclude that such a review would be unlikely to generate a surplus which could be applied to the delivery of affordable housing in future phases.

1.7 To put this in context my practice has dealt with several large schemes (1,000-6,000 units) in the last year or so where the agreed minimum delivery of affordable housing on sites has been in the range of 10%-20% of units. Only where a higher guaranteed affordable housing delivery is proposed and that is initially deemed unviable, has a post implementation review mechanism been foregone.

1.8 The Council's aspiration is to see this development expedited to increase supply in the local market. The best way to achieve that is to ensure that there is a viability review if the scheme has not been meaningfully implemented within a set period from the date planning consent is granted. I have recommended this type of mechanism on many schemes and notably it was accepted locally on the Wing development on the Cambridge City fringe. The applicant has agreed to the principle of this type of review and it is on that basis that I make the recommendation below.

1.9 I am therefore content to advise that the offer of 30% affordable housing is currently unviable, and that a review mechanism would not be appropriate in this instance.

2. Assessment methodology

2.1. The applicant's appraisal uses Turner Morum's residual land value model, which we have interrogated on numerous occasions over the last few years. I can confirm that it is an acceptable model for the purposes of the viability assessment.

2.2 Unit Mix

2. The scheme comprises 2,350 residential units and 13.04 Acres of employment land as set out in the accommodation schedule of the applicant's appraisal.

2.3 Values of residential units

2.3.1 The values used within the applicant's appraisal are based on the evidence of preceding phases built out by the applicant. It therefore provides a local evidence base which is robust.

2.3.2 The average value derived by TM is XXXX. From our checking of the local market, and considering the mix of unit types, this figure is appropriate.

2.3.3 The ground rent assumed by TM is XXXXXX. This figure is appropriate in the current market for the mix of units proposed. TM have then applied a yield of 5% to capitalise the ground rent income, which again is appropriate as it is close to the value obtained at recent auction sales. However, I note that they have not deducted any purchaser costs which would amount to 6.75% of the capital value. This is a small omission in cost terms at XXXX.

2.3.4 Turner Morum have provided details of two offers for the affordable housing from Havebury and BPHA. These are at XXXXXX Affordable Rented units and XXXXXX Shared Ownership units.

2.3.5 Notwithstanding these offers the applicant has advised TM that a level of XXXX has been achieved recently on a small scheme of 12 affordable houses and TM have adopted this level as a straight average for both tenures. This equates to 53.25% of open market value (OMV). We would normally expect to see 65% of OMV for Shared Ownership and 42% of OMV for Affordable rent which on a 50/50 tenure mix would make an average of 53.5% OMV, thus we believe the TM assumption to be realistic.

2.3.6 It should be noted that the above comments are based on the assumption that no grant or RP cross-subsidy is put into the value of the affordable housing. We would recommend that the delivery of the affordable housing is governed in the S.106 agreement on that basis. In that way if either grant or cross-subsidy is forthcoming then additional affordable housing should be delivered.

2.3.5 By combining the capital value of the apartments/houses and employment land with the ground rents gives a total gross development value (GDV). The estimate in the applicant's appraisal is XXXXXX which, in our opinion, is appropriate for the subject scheme.

2.4 Development Timescale

2.4.1 TM have defined the development timescale for pre-construction planning/building contractor selection, the building period, and the selling period as 16 years. Having reviewed the cash flow this period and the spread of income and expenditure over that period, is appropriate.

2.5 Build costs

2.5.1 The build costs provided by TM in their appraisal have been independently reviewed by the Council's consultant, Silver DCC.

2.5.2 Silver's initial review of the cost plan shows that the total cost for the scheme including base build cost, abnormal costs and infrastructure should be XXXX which is XXXX lower than that put forward by TM..

2.5.3 Silver and the applicants engaged in further discussions and the applicants increased their view of the base build cost by £9M, and lowered the infrastructure costs by £1.3M. Silver's reviewed these further costs and advised that they would anticipate the overall costs to be £13.6M lower than the revised estimate mainly because they did not agree all of the increase in the base build cost of the housing.

2.5.4 In this disagreement lies the central issue of the risks associated with large scale developments and the ability to agree minimum delivery of affordable housing at policy compliant level. Even if all of the suggested cost savings were achieved the scheme would only just be able to deliver affordable housing at the policy compliant level of 40%. However that needs to be taken in the context of the items I note below where the applicant has assumed costs less than the industry norm and therefore the viability would be worse if these were applied in full.

2.6 Other assumptions

2.6.1 Professional Fees – a figure of 2% has been used for professional fees by the applicant. This will vary according to the size and complexity of the scheme. We normally adopt 6-8% for large sites (with repetitive designs), 10-12% for complex sites (with a variety of different designs) and 10-15% for small sites, where the scale of the fees is larger due to the lower overall cost of build. The applicant's assumption is extremely low and if raised to the minima of 6% as noted above would make increase the scheme costs by £12.2M. This includes allowance for an arithmetic error made by TM when calculating the fees by £1.4M at the lower rate.

2.6.2 Sustainability - the applicant's original appraisal allowed for £345 per unit (a total of £811,500) for the increase in build cost to cover wheelchair housing and Lifetime Homes. Following comment by Silver DCC and Mr Ousby, this allowance has been removed from TM's final appraisal on the basis that building regulations have now moved on.

2.6.3 Contingency - the applicant's appraisal allows 3% for contingency in the build-up of the base costs. It would be normal to apply a figure of 5% to both the base build costs and infrastructure costs which would lead to an additional cost of £5.42M.

2.6.4 S.106 Contributions - Section 106 costs have been allowed in the sum of £61,024,628, which compares to a figure used by Mr Ousby of £57,135,042. The Council needs to confirm if the latter figure is correct. If so, this would go some way to closing the viability gap on the appraisal.

2.6.5 Sales and Marketing – 3.25% has been allowed for by the applicant, which in our view is low in the current market for this type of site. A more normal allowance for schemes of this size with multiple sales areas and relatively high promotion costs is in the order of 4-4.5%. Taking the lower end of this range would increase the scheme cost by £3.9M. In addition, the applicant has allowed for the affordable housing marketing and sale costs at 0.5% which we believe is acceptable. It should be noted that no separate fee for legal costs on sales has been applied. This would normally be allowed at circa £1,000 per open market unit.

4.6.6 Site acquisition costs – the applicant's site acquisition costs have been set within the normal range for this type of site, reflecting the increased cost of stamp duty to 6.75% in total.

2.6.7 Finance costs – an interest rate of 6% has been used by the applicant, which is within the range of current market activity (6-7% depending on whether arrangement and surveyors' fees are allowed for separately). The applicant has not allowed for arrangement fees or bank monitoring costs. These fees would add up to 1% in addition to the base interest rate, therefore a saving of £3.5M has been made.

2.6.8 Profit – the applicant has adopted a figure of 20% of GDV for the return for risk and profit on the open market sales. In addition they have allowed 6% of the value of the affordable housing as the profit for that element of the scheme and 15% of the value of the employment land.

We would note that Mr Ousby's appraisal adopts the same profit percentages, however with regard to the affordable housing the 6% profit is applied to the cost not the value, thus making a small saving. Whether profit should be applied to cost or value on affordable housing is very much in debate in the market, however I can comment that the majority of schemes we see apply it to the value.

Arundene Orchard Loxwood Road Rudgwick West Sussex RH12 3BT

e andy.leahy@bpglimited.co.uk t 01403 823425 f 01403 824075 w www.bpglimited.co.uk

In respect of the open market housing profit a lot has changed this year. Whereas early in 2016 a profit of 18% would have been acceptable on a site such as this where the local market is well known by the applicant, the changes to Stamp Duty, increased status criteria for mortgages, and the Brexit Referendum have combined to increase the anticipated risks moving forward. As an example the additional 3% stamp duty on buy to let purchases combined with reductions in mortgage offset relief on rental income has caused a reduction in consumer confidence in this area of the market where up to 30% of open market sales have previously been targeted.

2.6.9 Other variables used by the applicant are minor in nature and reflective of scheme type, size and current market conditions.

2.7 Benchmark Land Value

2.7.1 TM has based their assessment of viability on a benchmark land value of XXXX per gross acre. This is an opinion of value based on TM's experience of the land market. I can confirm as set out in our original report of March 2016 we are satisfied that this level of land value is both appropriate for the type of site, scheme size and the delivery of a return to the land owner as required under para 173 of the NPPF.

3. Conclusion

3.1 It can be seen from the above assessment that the scheme as proposed, with 30% affordable housing is currently unviable as it shows a deficit of XXXX against the benchmark land value.

3.2 I have identified a number of items in the applicant's appraisal which have been under costed and thus if applied at market rates the appraisal more unviable:

3.3 Taking account of the above viability position in the current market and Mr Ousby's assessment which shows a worse position, I can advise that the use of a viability review mechanism in this case is unlikely to lead to a surplus being generated at a future date in order to generate additional affordable housing above the 30% offered.

3.4 The balance between asking for a review mechanism with a lower level of affordable housing and securing a guaranteed higher level of affordable housing is a matter for decision makers to weigh up.

Should you have any queries on the above, please do not hesitate to contact me. I look forward to seeing you at the planning committee in the new year.

Arundene Orchard Loxwood Road Rudgwick West Sussex RH12 3BT

e andy.leahy@bpglimited.co.uk t 01403 823425 f 01403 824075 w www.bpglimited.co.uk

Yours sincerely

A M LEAHY
Managing Director

Arundene Orchard Loxwood Road Rudgwick West Sussex RH12 3BT

e andy.leahy@bpglimited.co.uk t 01403 823425 f 01403 824075 w www.bpglimited.co.uk