

For: Havant Borough Council Review of Applicant Submitted Viability Position

**Wellington Way
Waterlooville
Hampshire
PO7 7EE**

**November 2019
(DSP19403P)**

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1. Notes and Limitations

- 1.1.1 The following does not provide formal valuation advice. This review and its findings are intended purely for the purposes of providing Havant Borough Council (HBC) with an independent check of, and opinion on, the planning applicant's viability information and stated position in this case.
- 1.1.2 This document has been prepared for this specific reason and should not be used for any other purpose without the prior written authority of Dixon Searle Partnership Ltd (DSP); we accept no responsibility or liability for the consequences of this document being used for a purpose other than for which it was commissioned. To the extent that the document is based on information supplied by others, Dixon Searle accepts no liability for any loss or damage suffered by the client.
- 1.1.3 We have undertaken this as a desktop exercise as is appropriate for this stage and level of review. For general familiarisation we have considered the site context from the information supplied by the Council and using available web-based material.
- 1.1.4 So far as we have been able to see, the information supplied to DSP to inform and support this review process has not been supplied by the prospective / current planning applicant on a confidential basis. However, potentially some of the information provided may be regarded as commercially sensitive (for example the estate agent valuation which are stated to be provided on a confidential basis). Therefore, we suggest that the Council and prospective / current or subsequent planning applicant may wish to consider this aspect together. DSP confirms that we are content for our review information, as contained within this report, to be used as may be considered appropriate by the Council (we assume with the applicant's agreement if necessary). In looking at 'Accountability' the July 2018 published revised national Planning Practice Guidance (PPG) on viability says on this; *'Any viability assessment should be prepared on the basis that it will be made publicly available other than in exceptional circumstances.'*
- 1.1.5 Dixon Searle Partnership conducts its work only for Local Authorities and selected other public organisations. We do not act on behalf of any development interests. We have been and are involved in the review of other planning stage proposals as well as strategic policy level assessment work within the HBC area.

- 1.1.6 In any event we can confirm that no conflict of interests exists, nor is likely to arise given our approach and client base. This is kept under review. Our fees are all quoted in advance and agreed with clients on a fixed or capped basis, with no element whatsoever of incentive/performance related payment.

2. Introduction

- 2.1.1 Dixon Searle (DSP) has been commissioned by Havant Borough Council (HBC) to carry out an independent review of the Economic Viability Appraisal (EVA) supplied to the Council on behalf of the applicant by Tangent Chartered Surveyors Ltd (TCS). This is in relation to the proposed development at Wellington Way, Waterloooville.
- 2.1.2 The viability information has been supplied in support of planning application reference APP/18/00234, for the demolition of existing shopping parade and redevelopment of the site to provide a nine-storey building consisting of 264 no. 1-bed / studio build to rent apartments with associated amenity facilities, car parking landscaping and an A2 unit (financial and professional services). Also, in regard to ref. APP/19/00513, for the erection of a three-storey multi-storey car park to provide 263 car parking spaces. The application for flats has been submitted in full and was validated on 13 March 2019.
- 2.1.3 The Council's core strategy policy CS9 requires the provision of between 30% and 40% affordable housing on site. The Council's Draft Local Plan 2036 states that town centre sites should be able to include 20% affordable housing.
- 2.1.4 The planning application is for a Build to Rent (BTR) scheme. The revised National Planning Policy Framework (NPPF) indicates that affordable housing in BTR schemes should normally be provided in the form of 'affordable private rent' (APR), and the associated guidance suggests that the inclusion of 20% APR in a BTR scheme is a suitable benchmark; but that local authorities can set a different proportion in local plan policy if justified by local housing need (and with reference to viability).
- 2.1.5 In this case, we understand that the scheme should provide 53 affordable homes based upon the Council's current policy.
- 2.1.6 In presenting their viability position, the applicant has supplied to the Council the aforementioned EVA dated 5 February 2018, and an updated EVA dated 23 August 2019, along with an electronic copy of a development appraisal carried out utilising the Housing Corporation Economic Assessment Tool, plus an appendix setting out development assumptions.
- 2.1.7 DSP has also had sight of the Council's online planning application file.

- 2.1.8 For general background, a viable development could be regarded as the ability of a development project to meet its costs including the cost of planning obligations, while ensuring an appropriate site value (i.e. existing use value) for the landowner and a market risk adjusted return to the developer in delivering that project. The Government's Planning Practice Guidance on Viability sets out the main principles for carrying out a viability assessment. It states:

'Viability assessment is a process of assessing whether a site is financially viable, by looking at whether the value generated by a development is more than the cost of developing it. This includes looking at the key elements of gross development value, costs, land value, landowner premium, and developer return...Any viability assessment should follow the government's recommended approach to assessing viability as set out in this National Planning Guidance and be proportionate, simple, transparent and publicly available. Improving transparency of data associated with viability assessment will, over time, improve the data available for future assessment as well as provide more accountability regarding how viability informs decision making...In plan making and decision making viability helps to strike a balance between the aspirations of developers and landowners, in terms of returns against risk, and the aims of the planning system to secure maximum benefits in the public interest through the granting of planning permission'¹.

- 2.1.9 Under normal circumstances, if the residual land value (RLV) created by a scheme proposal exceeds the existing use value plus a premium (referred to as a benchmark land value (BLV) in this case) then we usually have a positive viability scenario – i.e. the scheme is much more likely to proceed (on the basis that a reasonable developer profit margin is also reached).
- 2.1.10 As discussed above, the planning application is for a Build to Rent (BTR) scheme. The principal difference between BTR and other tenures is that BTR schemes are financed via a long-term investment approach (for example usually backed by a pension fund or similar). All homes in a scheme remain in the same ownership and are managed as one investment, usually without the involvement of a Registered Provider of affordable housing (e.g. a housing association).

¹ <https://www.gov.uk/guidance/viability#viability-and-decision-taking>

- 2.1.11 The submitted plans indicate that the flats are aimed at young professionals and, similarly to other Build to Rent proposals around the country, feature communal facilities such as a shared lounge, cinema and car club.
- 2.1.12 In this case the submitted development appraisal has been run to determine the residual value after allowing for a fixed profit of 15% on cost, which is stated to equate to 12.44% GDV. This residual value has then been compared to a benchmark land value, based on the existing use of the site. Therefore, an approach has been taken that sets out to consider, in the applicant's view, the maximum supportable financial contribution for affordable housing.
- 2.1.13 The 2018 EVA states that scheme without any affordable housing or any other S106 contribution has a residual value of £94,725, and therefore shows a deficit of -£2,865,275 against the stated benchmark land value of £2,960,000. The update to the EVA includes values and costs for a multi-storey car park, which results in a residual value of £814,635, thus improving the viability position but nonetheless showing a deficit of £2,145,365.
- 2.1.14 On this basis the EVA concludes that: *"the project clearly cannot support any additional s106 contributions in particular for affordable housing."*
- 2.1.15 The EVA as presented (flats only) assumes a developer's profit of £3,927,934 set against a deficit of -£2,865,275, therefore an overall profit position (landowner/developer) of £1,062,659 or 3.5% of the gross development value of £30,800,088.
- 2.1.16 The updated 2019 EVA assesses the scheme including a multi-storey car park on a separate site, and a combined profit for the two sites of £4,311,463 is shown, which is compared with the same BLV, therefore an overall profit position of £2,166,098 or 6.3% of GDV.
- 2.1.17 The EVAs state that the developer aims to resolve the significant deficit through *"improvements in Investment Yield and reduction in delivery costs"*, and by *"undertaking the scheme on a significantly reduced development profit"*.
- 2.1.18 This review does not seek to pre-determine any Council positions, but merely sets out our opinion on the submitted viability assumptions and outcomes in order to inform the

Council's discussions with the applicant and its decision making; it deals only with viability matters, in accordance with our instructions.

- 2.1.19 Havant Borough Council requires our opinion as to whether the viability figures and position put forward by the applicant are reasonable. We have therefore considered the information submitted. Following our review of the key assumptions areas, this report provides our views.
- 2.1.20 We have based our review on the submitted Economic Viability Appraisals (EVA) and the premise that the viability of the scheme should be considered based on the assumption of current costs and values. We then discuss any variation in terms of any deficit (or surplus) created from that base position by altering appraisal assumptions (where there is disagreement if any).
- 2.1.21 As a consultancy, DSP have a considerable track record of assessing the viability of schemes and assessing the scope for Local Authority planning obligation requirements. This expertise includes viability-related work carried out for many Local Authorities nationwide over the last 16 years or so, including in Surrey and the surrounding areas.
- 2.1.22 The purpose of this report is to provide our overview comments with regard to this individual scheme, on behalf of the Council - taking into account the details as presented. It will then be for the Council to consider this information in the context of the wider planning objectives in accordance with its policy positions and strategies.
- 2.1.23 The review does not seek to pre-determine any Council positions, but merely sets out our opinion on the submitted viability assumptions and outcomes in order to inform the Council's discussions with the applicant and its decision making; it deals only with viability matters, in accordance with our instructions.
- 2.1.24 In carrying out this type of review a key theme for us is to identify whether, in our opinion, any key revenue assumptions have been under-assessed (e.g. sales value estimates) or any key cost estimates (e.g. build costs, fees, etc.) over-assessed – since both of these effects can reduce the stated viability outcome.

3. Review of Submitted Viability Assumptions

- 3.1.1 The following commentary reviews the applicant's submitted viability appraisal assumptions as explained within the EVA and related development appraisal.
- 3.1.2 Primarily the review process considers the fact that the collective impact of the cost and value assumptions is of greatest importance, rather than the individual detailed inputs in isolation. We have considered those figures (the appraisal assumptions) provided and reviewed the impact of trial changes to the submitted assumptions where our opinion differs to that presented in the EVA.
- 3.1.3 This type of audit / check is carried out so that we can give the Council a feel for whether or not the indicated profit positions are approximately as expected – i.e. informed by a reasonable set of assumptions and appraisal approach.
- 3.1.4 Should there be changes to the scheme proposals this would obviously impact on the appraisal outputs.

Benchmark Land Value (BLV)

- 3.1.5 In all appraisals of this type, the base value (value of the site or premises – e.g. in existing use) is one of the key ingredients of scheme viability. A view needs to be taken on this so that it is sufficient to secure the release of the site for the scheme (sale by the landowner) but is not assumed at such a level that restricts the financial capacity of the scheme to deliver suitable profits (for risk reward), cover all development costs (including any abnormals) and provide for planning obligations as a part of creating sustainable development. This can be a difficult balance to reach, both in terms of developers' dealings with landowners, and Councils' assessments of what a scheme has the capacity to bear.
- 3.1.6 The RICS Guidance 'Financial viability in planning'² states that:

'A viability appraisal is taken at a point in time, taking account of costs and values at that date. A site may be purchased some time before a viability assessment takes place and circumstances might change.'

² RICS Professional Guidance – Financial viability in planning (August 2012)

This is part of the developer's risk. Land values can go up or down between the date of purchase and a viability assessment taking place; in a rising market developers benefit, in a falling market they may lose out.

A developer may make unreasonable/overoptimistic assumptions regarding the type and density of development or the extent of planning obligations, which means that it has overpaid for the site'.

3.1.7 The revisions to the 'Viability' section of the PPG and the new NPPF (Updated 19.02.2019) now very clearly advise that land value should be based on the value of the existing use plus an appropriate level of premium or uplift to incentivise release of the land for development from its existing use. With regard to how land value should be defined for the purpose of viability assessment it states *'To define land value for any viability assessment, a benchmark land value should be established on the basis of the existing use value (EUV) of the land, plus a premium for the landowner.'*

3.1.8 The guidance defines existing use value as: *'the first component of calculating benchmark land value. EUV is the value of the land in its existing use together with the right to implement any development for which there are policy compliant extant planning consents, including realistic deemed consents, but without regard to alternative uses. Existing use value is not the price paid and should disregard hope value. Existing use values will vary depending on the type of site and development types. EUV can be established in collaboration between plan makers, developers and landowners by assessing the value of the specific site or type of site using published sources of information such as agricultural or industrial land values, or if appropriate capitalised rental levels at an appropriate yield. Sources of data can include (but are not limited to): land registry records of transactions; real estate licensed software packages; real estate market reports; real estate research; estate agent websites; property auction results; valuation office agency data; public sector estate/property teams' locally held evidence.'*

3.1.9 It states that a Benchmark Land Value should:

- *'be based upon existing use value*
- *allow for a premium to landowners (including equity resulting from those building their own homes)*
- *reflect the implications of abnormal costs; site-specific infrastructure costs; and professional site fees and*

- *be informed by market evidence including current uses, costs and values wherever possible. Where recent market evidence is used to inform assessment of benchmark land value this evidence should be based on developments which are compliant with policies, including for affordable housing. Where this evidence is not available plan makers and applicants should identify and evidence any adjustments to reflect the cost of policy compliance. This is so that historic benchmark land values of non-policy compliant developments are not used to inflate values over time.'*

3.1.10 It further states that: *'Where viability assessment is used to inform decision making under no circumstances will the price paid for land be a relevant justification for failing to accord with relevant policies in the plan.'* It goes on to state: *'Policy compliance means that the development complies fully with up to date plan policies including any policy requirements for contributions towards affordable housing requirements at the relevant levels set out in the plan. A decision maker can give appropriate weight to emerging policies. Local authorities can request data on the price paid for land (or the price expected to be paid through an option or promotion agreement.)'*

3.1.11 In regard to assuming an alternative use value to determine BLV the guidance states: *'For the purpose of viability assessment alternative use value (AUV) refers to the value of land for uses other than its current permitted use, and other than other potential development that requires planning consent, technical consent or unrealistic permitted development with different associated values. AUV of the land may be informative in establishing benchmark land value. If applying alternative uses when establishing benchmark land value these should be limited to those uses which have an existing implementable permission for that use. Where there is no existing implementable permission, plan makers can set out in which circumstances alternative uses can be used. This might include if there is evidence that the alternative use would fully comply with development plan policies, if it can be demonstrated that the alternative use could be implemented on the site in question, if it can be demonstrated there is market demand for that use, and if there is an explanation as to why the alternative use has not been pursued. Where AUV is used this should be supported by evidence of the costs and values of the alternative use to justify the land value. Valuation based on AUV includes the premium to the landowner. If evidence of AUV is being considered the premium to the landowner must not be double counted.'*

- 3.1.12 It is therefore clear that the only acceptable approach to defining a benchmark land value for the purposes of a viability assessment, is the EUV+ or exceptionally AUV.
- 3.1.13 In this case, the benchmark is based on an assessment of the value of the housing site in its existing use as 18 retail units (some of which “have been allowed to become vacant” due to the site being earmarked for development, and some of which have been combined over time to provide larger shops). The assessment also includes the value/costs of a proposed multi-storey car park which is to be built on a separate site which is currently a council-owned surface car park. The updated EVA states that ‘no [land] cost allowance has been made for the car park site’. The valuation of the multi-storey car park for the purposes of the EVA includes an assessment of the value of the existing council-owned car park, concluding that its existing use value is £1,011,769. If this amount were added to the EUV/BLV it would further reduce the overall profit position to circa 3% of GDV. We are not aware of how this car park is being treated by the Council, i.e. whether a capital receipt is expected for the land, or if this is being included to enable development/town centre regeneration.
- 3.1.14 The existing units consist of a total of 22,642 sq ft of commercial space, built in 1982, and valued at a rental value of £257,450 (£11.37 psf). This has been capitalised using a yield of 10% resulting in an EUV of £2,574,500.
- 3.1.15 A tenancy schedule has been supplied for the shopping centre (including units outside the site boundary) which has a total internal area of 55,309 sq ft and income of £664,056, therefore (at the time the schedule was produced) a rate of £12.01 psf.
- 3.1.16 We have conducted our own research using the Co-Star commercial database, and the results indicate that rent levels are within the expected range (examples attached as Appendix 1 to this report). However, this assumes there is demand for the units and that they are in a suitable condition to let.
- 3.1.17 We have also reviewed retail units available to let in WaterlooVille currently (attached as Appendix 2) which indicate an average rent of £13.41 (with lower rents advertised at the end of London Road, away from the main shopping precinct).

Asking price	Size (sq ft)	£ psf
£ 12,000	1194	£ 10.05
£ 17,000	2447	£ 6.95
£ 15,000	1570	£ 9.55
£ 15,000	1607	£ 9.33
£ 40,000	2404	£ 16.64
£ 62,500	2823	£ 22.14
AVERAGE		£ 13.41

3.1.18 Overall we consider that the rental assumption of £11.37 psf is not unreasonable.

3.1.19 A premium of 15% has been added to the EUV to incentivise development, resulting in a BLV of £2,960,000.

3.1.20 The condition of the units externally and the area generally is poor, and as stated in the EVA, one third of the units are vacant. There appears to have been a lack of investment in the units, and a number of units left long-term vacant, due to the development proposals. Any new lessee would have to invest in fitting out/updating the interior. Town centre units are also in competition with the newer out of town shopping area to the north west of the town, with vacant units in the main shopping precinct as well as in Wellington Way. This combined with the difficulties faced by high street shops generally raises the question of whether full occupation of the units can be achieved, and what the interest would be from potential investors if the whole site was offered to the market in its existing use.

3.1.21 Overall, we consider the assumed EUV of £2,274,500 to be acceptable, however the premium of 15% appears excessive as the units are in need of investment and there is low demand for units in Waterlooville town centre currently. It could be argued that no premium is required to incentivise the owner to sell for housing development, however at this stage we have allowed a 10% premium in this case, thus a BLV of £2,501,950.

Acquisition costs

3.1.22 Acquisition costs have been applied, and include £137,500 in SDLT. We have verified this sum using the HMRC stamp duty calculator based on the BLV of £2,960,000. Based on our suggested BLV of £2,501,950 the SDLT is £114,597.

3.1.23 £59,200 has been included for land valuation/agents'/legal fees. This latter amount equates to approximately 2% of the BLV. We consider these costs to be within reasonable parameters.

- 3.1.24 £150,000 has also been included as a cost for 'Statutory Compensation etc'. This is an expense that will have to be incurred in order to proceed with the development, and does not appear an unreasonable sum. However, we do not have details of the amounts that will have to be paid to end the leases and for completeness the Council may wish to verify these costs with the applicant.

Gross Development Value – Private Residential

- 3.1.25 The proposed development is of 254 standard flats of and 10 disabled flats, totalling 9,670m². The disabled flats are 30m². Each standard flat is 26.88m² and has been valued at £121,739 based on a rental income of £170 per unit per week, with an occupancy level of 50 weeks per annum (gross rent of £8,500 per studio flat)³.
- 3.1.26 Running costs have been assumed at £1,500 per unit per annum, therefore net rental income is assumed to be £7,000 per unit per annum. This has been capitalised at a rate of 5.75%, to produce an overall value for the units of £32,139,096.
- 3.1.27 We have carried out research into rents locally, which indicates that the average rent for a studio/1-bed flat in Waterlooville is £150 per week. In our experience, BTR developments which offer purpose-built accommodation with communal facilities can be expected to achieve around 20% above the market rate per bed, which would indicate a rent of £180 per week. In this particular location the potential rent will be affected by the lack of a railway station, which is generally seen as an important factor for a BTR development. Residents who are not working locally will be reliant on buses, or will have to own a car (with the capacity for car parking in the immediate area, even with the new car park, being severely limited). Similarly, the development is not close to a university, or even the local colleges which in any case will be mainly attended by students living at home. Taking into account the downward effect of these factors on the potential rent, we consider the proposed figure of £170 per week to be a not unreasonable assumption.
- 3.1.28 We note also that the nearby Berewood development featured Build to Rent properties, including 1 bed flats (larger than the proposed flats, not studios) which were recently let at £825pcm (£190 per week), which further indicates that £170 per week is a suitable rent level.

³ Can also be seen as a gross rent of £8,840 per property, less £340, or 4% for voids.

Watson Lane, Berewood



- Rented and archived

- LET











£825 pcm

Fees apply

First Floor Flat

 **Waterlooville:**
023 92647 171

 **Enquire about property**

 **Book a viewing**

 **Tell a friend**

 **View map**

Features

 One Bedroom
 Balcony

 First Floor Apartment

 One Allocated Parking Space

3.1.29 A yield of 5.75% has been applied to the net rent for the 264 flats to arrive at a per unit value of £116,667. The explanation for this choice of yield rate is that *“published research by Knight Frank suggests Investment Yields for Secondary Regional Cities to be 5.25%. Waterlooville is not a Secondary Regional City and as such [...] an investment yield of 6% is appropriate for this project taking into account the location of the site and transport links.”*

3.1.30 The source of the Knight Frank research referred to in the EVA is not given but appears to be a residential yield guide⁴ which provides yields for “London and the South East” and for “Secondary Regional Cities”. It also includes the following notes: *“Yields in the London and South East categories are reflective of income-focused transactions of institutional assets. Regional locations: We have provided an indication of yields in respect of a number of example locations, illustrating the spread of yields in this classification. These yields are reported in respect of institutional quality, stabilised*

⁴ <https://content.knightfrank.com/research/588/documents/en/uk-residential-investment-yield-guide-october-2019-6728.pdf>

assets.” The guide suggests 5% to 5.25% for Secondary Regional Cities, with the market sentiment being “POSITIVE”, i.e. likely to lead to falling yields.

- 3.1.31 We consider the category of ‘London and South East’ to be a more suitable guide, which Knight Frank suggests a yield of 4.0% to 4.25%. The South East is known to be ‘high value, low yielding’ in comparison to the rest of the UK. The relatively low rents for Waterlooville (discussed above) compared to other parts of Hampshire take account of the location of the site and transport links. Waterlooville cannot be considered ‘Prime’, however the scheme is presented as a Build to Rent investment aimed at Pension Funds and other institutional investors, and our research into Build to Rent schemes and experience of other schemes in the South East suggests a net initial yield of between 4% and 5% or between 6% and 7% based on gross rent.
- 3.1.32 L&Q, a housing association with a private rented sector (BTR) arm, reported in 2018 that it was achieving net rental yield of 4.2% (gross yield of 5.5%)⁵.
- 3.1.33 Savills’ “Investing in private rent” report from 2018 stated that *“net initial yields on BTR deals averaged 4.3% between 2015 and 2017. But that hides substantial regional variation. While half that investment took place in London, where yields averaged 3.8 per cent, across Scotland and the north of England the average yield was 4.9 per cent”*. The CIO of Cortland (a major US investor in the UK BTR market) is quoted as saying *“Net yields on UK BTR are around 4%”*⁶.
- 3.1.34 If the developer is prepared to proceed with the scheme as build to rent it has to be assumed that a market has been identified for it, with a similar level of risk to other BTR developments. The viability of this proposal is highly sensitive to the yield rate used to capitalise rental value. As far as we are aware there is no precedent for a BTR development of this scale in a similar location. Reviewing the above, we consider a yield of 6% of net rent to be excessive, and have tested a yield of 5%, which is higher than the yield assumed for more centrally located BTR schemes (and also higher than yields normally expected from standard buy to let investments in the South East, which are typically below 4%, due to the high price of property in relation to achievable rent). A 5% yield produces a development value of £36,960,000, increasing the GDV of the scheme by £4.8 million.

⁵ Source: Social Housing Insight, (socialhousing.co.uk)

⁶ <https://www.bisnow.com/london/news/multifamily/what-does-2019-have-in-store-for-uk-build-to-rent-96798>

- 3.1.35 It is worth noting that any improvement in the rental value assumptions (compared with a level set at the point of the appraisal) would most likely be reflected in an improvement in scheme viability. Whilst the opposite could also occur (the rental values could fall relative to the assumptions made), that is the developer's (applicant's) risk and such factors need to be kept in mind in making an overall assessment of the applicant's position.

Gross Development Value - Affordable Housing

- 3.1.36 Affordable units have not been included in the submitted appraisal, therefore we have not reviewed this element.

Gross Development Value – Car Park

- 3.1.37 A valuation has been provided of the existing car park (for information only, as this has not been added to the EUV). The details of the valuation of the proposed car park have not been discussed, however it would appear that the per bay rate from the EUV calculation (£10,650 per space) has been applied to the proposed 263 spaces to arrive at a development value of £2,513,400.
- 3.1.38 The per bay rate has been based on an assumed income of £117,748 for 95 spaces, with deductions for maintenance and running costs, as well as operator's profit at 15%, capitalised at a yield of 7%. We consider the assumptions made to be not unreasonable and the capitalised value is within the typical range for similar car parks in 'fringe' town centre shopping locations. Overall, we do not consider the value to be unfairly assessed.
- 3.1.39 It is not clear on what basis the 139 spaces stated to be allocated for the use of residents of the BTR development (subject to take-up) will be charged to tenants, however if provided on a season ticket basis the overall income will be likely to reduce thus worsening the viability of the scheme.
- 3.1.40 The assumed cost of building the car park (£3,511,000 including external/abnormal works) exceeds the value of the completed car park, and taking into account the stated EUV of the existing surface car park, the multi-storey car park on its own shows a deficit of -£2,009,369. Clearly the car park has been added to the planning application in order to mitigate concerns raised about the original application and the lack of associated parking, and the position as presented indicates that the multi-storey car park has to be subsidised by the residential element of the scheme.

Development Timings

- 3.1.41 The development timings set out in the EVA indicate a total development period of 20 months with a 3-month lead-in from site acquisition followed by a 17-month build period with sales occurring immediately on completion – the development being sold to a long-term investor.
- 3.1.42 Overall, these development timings appear reasonable in our opinion.

Build costs - Flats

- 3.1.43 The EVA uses an overall base build cost of £1,839/m² for the flats, stated to be based on a BCIS median rate “for PRS schemes”, and £550/m² for the ground floor parking (undercroft) areas (217m²) beneath the residential accommodation. In our opinion, this type of development sits somewhere between the two BCIS categories of student residences and general flatted development. As noted above, the EVA refers to the proposed accommodation as ‘student halls’ and the size of the proposed properties (27m²) is more typical of student accommodation. However the flats are self-contained and the development is stated to be aimed at young professionals; it seems unlikely that many students would live in this location which is some distance from the University. The internal area of the development is 73% of the gross area; this is a lower percentage than for standard flatted development, but is again more typical to student development than BTR development which can involve an even larger proportion of communal space.
- 3.1.44 We have reviewed the BCIS rates for both flatted and student accommodation (rebased to a Havant location factor) which are as follows:

Results

> Rebased to Havant (112; sample 22) Edit

£/m2 study

Description: Rate per m2 gross internal floor area for the building Cost including prelims. ?

Last updated: 26-Oct-2019 00:38

Maximum age of results: 5 years ▼

Building function (Maximum age of projects)	£/m² gross internal floor area						Sample
	Mean	Lowest	Lower quartiles	Median	Upper quartiles	Highest	
New build							
816. Flats (apartments)							
Generally (5)	1,651	940	1,348	1,521	1,822	5,751	238
1-2 storey (5)	1,628	1,071	1,346	1,541	1,850	2,689	63
3-5 storey (5)	1,591	940	1,328	1,485	1,752	3,641	153
6 storey or above (5)	2,132	1,262	1,676	1,820	2,092	5,751	22
856.2 Students' residences, halls of residence, etc (5)	2,002	1,230	1,819	2,048	2,261	2,463	17

3.1.45 The submitted build cost of £1,839/m² slightly higher than the “6-storey and above” median rate (5 yrs) – however we note that the rate of construction for “Students’ residences” is significantly higher. As such we consider it to be a not excessive estimate for base build costs in this case.

3.1.46 The rate of £550/m² for undercroft parking provision is approximately 30% of the build cost rate for the flats, and is within the expected range.

External/Abnormal costs

3.1.47 Constructions costs over and above the BCIS rate are described as follows:

Over Extra Construction Costs	m2	£/m2	£
Podium Deck area	348	£ 100	£ 34,800
Roof Terrace	314	£ 100	£ 31,400
Demolition	2,613	£ 45	£ 117,585
Utility Infrastructure Charges			£ 237,600
Incoming Services			£ 20,000
Foul Drainage			£ 20,000
Surface Water Drainage			£ 20,000
Off Site Works	200	£ 120	£ 24,000
Euro Bins	33 bins	£250 per bin	£ 8,250
Hard Surfaces	200	£ 80	£ 16,000
RenewableEnergy			£ -
ServiceDiversion			£ -
Over Extra Foundations			£ -
TOTAL			£ 529,635

3.1.48 Given the area of buildings to be demolished and their proximity to other buildings/businesses the demolition costs appear not unreasonable. The other major item in the list is 'Utility Infrastructure Charges' which again are within expected parameters for the addition of such a large number of flats. Overall, the costs for construction of the flats do not appear excessive.

Build costs – car park

3.1.49 The car park is stated to have a GIA of 5,562m², and is costed at a rate of £618/m², providing a total of 263 spaces across three levels. 139 spaces are stated to be for use by residents of the proposed BTR scheme.

3.1.50 The following external/abnormal costs are included for the car park:

Car Park Construction - External/Abnormal Costs		
Landscaping	£	5,000
Services	£	5,000
External Bays	£	16,474
External Road	£	37,210
Car Park SWD	£	10,000
TOTAL	£	73,684

3.1.51 Base build cost is assumed to be £618/m² (which is within the range suggested by BCIS), thus the total build cost (including external/abnormal works) assumed for the car park is £3,511,000 or £13,350 per space. Overall we consider these costs to be within expected parameters.

Contingency and Professional Fees

3.1.52 The development appraisal accompanying the EVA includes an allowance for contingencies of 5%. This is a fairly standard and acceptable assumption.

3.1.53 7% has been included for professional fees. Again, this is not outside normal market parameters and is considered a suitable assumption.

Cost Assumptions – CIL/Section 106 Payments

3.1.54 Although the conclusions of the EVA state that no S106 contributions can be supported by the scheme, a sum of £99,000 has been allowed for S106 costs within the appraisal (£375 per flat for habitat mitigation). £761,097 has been allowed for Community

Infrastructure Levy (CIL) based on a net increase in area of £7,057m² and an indexed rate of £107.85/m².

- 3.1.55 Any contributions sought would have an impact on the overall viability of the scheme as viewed through the appraisal. Therefore, we recommend the Council verifies the assumed CIL contributions and any S106 payments required. We note that in addition to the habitat mitigation mentioned in 3.1.54, above, contributions towards nutrient neutrality will be required in order for the development to go ahead, and this will have an impact on the viability of the scheme.

Development Finance

- 3.1.56 Finance costs have been included using a rate of 5% (comprised of arrangement fees of 1% and interest rates of 4%).

- 3.1.57 The interest rate is the cost of funds to the scheme developer; it is applied to the net cumulative negative cash balance each month on the scheme as a whole. According to the HCA in its notes to its Development Appraisal Tool (DAT): *'The rate applied will depend on the developer, the perceived scheme risk, and the state of the financial markets. There is also a credit interest rate, which is applied should the cumulative month end balance be positive. As a developer normally has other variable borrowings (such as an overdraft), or other investment opportunities, then the value of credit balances in reducing overall finance charges is generally the same as the debit interest charge. A zero rate of credit interest is not generally plausible and will generate significantly erroneous results in a long-term scheme.'*

- 3.1.58 RICS also points out that it is often the case that schemes are modelled at current costs & values i.e. ignoring inflation (as is the case here). In this case RICS Financial Viability in planning paper states in appendix D 4.5 *'... current values and costs should be used together with a **net** of inflation finance rate. Such a net of inflation rate would be much lower than a bank rate (which naturally includes inflation expectations).'*

- 3.1.59 We consider the submitted rate of 5% interest on land and construction costs to be a suitable assumption.

Cost Assumptions - Sales & Marketing Fees and Legal Fees

- 3.1.60 The EVA includes sales fees of 1.5%. This is a 100% rented scheme so there should not be sales fees. There will be marketing and letting fees in connection with the rented

properties, but these would normally form part of the running cost already accounted for (see 3.1.26). We question, therefore, whether this item (amounting to £519,787) should be included as a cost.

- 3.1.61 Purchaser's Costs relating to the sale of the BTR scheme are included at 5.8% of the GDV of the units (total of £1,864,068) which is stated to include SDLT. This does not exceed the costs we would expect to see for the sale of this type of investment.

Developer's risk reward – profit

- 3.1.62 In this case, the level of profit has been included as a fixed input at 15% of cost, which in this case equates to 12.44% of GDV. The level of profit assumed viable is a matter of debate but in our experience of build to rent schemes (and having consulted across the build to rent sector as part of a study looking specifically into the viability of this tenure) a profit level of 10% of GDV for PRS units (and up to 12% on cost) is considered acceptable to applicants, alongside 6% on GDV for 'affordable private rented' units.
- 3.1.63 The RICS Guidance states that: *'When a developer's return is adopted as the benchmark variable, a scheme should be considered viable, as long as the cost implications of planning obligations are not set at a level at which the developer's return (after allowing for all development costs including site value) falls below that which is acceptable in the market for the risk in undertaking the development scheme. If the cost implications of the obligations erode a developer's return below an acceptable market level for the scheme being assessed, the extent of those obligations will be deemed to make a development unviable as the developer would not proceed on that basis'.*
- 3.1.64 It goes on to state: *'The benchmark return, which is reflected in a developer's profit allowance, should be at a level reflective of the market at the time of the assessment being undertaken. It will include the risks attached to the specific scheme. This will include both property-specific risk, i.e. the direct development risks within the scheme being considered, and also broader market risk issues, such as the strength of the economy and occupational demand, the level of rents and capital values, the level of interest rates and availability of finance. The level of profit required will vary from scheme to scheme, given different risk profiles as well as the stage in the economic cycle. For example, a small scheme constructed over a shorter timeframe may be considered relatively less risky and therefore attract a lower profit margin, given the exit position is more certain, than a large redevelopment spanning a number of years where the outturn*

is considerably more uncertain. A development project will only be considered economically viable if a market risk adjusted return is met or exceeds a benchmark risk-adjusted market return’.

3.1.65 Planning Practice Guidance on Viability states (our underlining): *‘Potential risk is accounted for in the assumed return for developers at the plan making stage. It is the role of developers, not plan makers or decision makers, to mitigate these risks. The cost of fully complying with policy requirements should be accounted for in benchmark land value. Under no circumstances will the price paid for land be relevant justification for failing to accord with relevant policies in the plan’.* It goes on to state: *‘For the purpose of plan making an assumption of 15-20% of gross development value (GDV) may be considered a suitable return to developers in order to establish the viability of plan policies. Plan makers may choose to apply alternative figures where there is evidence to support this according to the type, scale and risk profile of planned development. A lower figure may be more appropriate in consideration of delivery of affordable housing in circumstances where this guarantees an end sale at a known value and reduces risk. Alternative figures may also be appropriate for different development types’.*

3.1.66 In our experience 15% profit on cost exceeds the profit assumed for this type of development, particularly when a contingency of 5% on cost has already been included to mitigate the risk of development. We consider 12% on cost to represent a suitable level of profit.

⁷ <https://www.gov.uk/guidance/viability#standardised-inputs-to-viability-assessment> - Paragraph: 018 Reference ID: 10-018-20190509

4. Summary and Recommendations

- 4.1.1 The overall approach to assessing the viability of the proposed development is appropriate in our opinion. The majority of the assumptions appear fair at this stage. The main point we have queried is the yield applied to the rental income. The EVA uses a 6% yield to capitalise the net annual rent, whereas in our experience net yield is typically assumed to be below 5% for BTR schemes.
- 4.1.2 We have tested a 5% yield, which produces a development value of £36,960,000, increasing the GDV of the scheme by £4.8 million, thus moving the scheme from a deficit against the stated BLV to a surplus of £2.68 million, whilst maintaining the suggested profit level 15% on cost (which using our updated assumption on development value equates to a profit of 10.9% on GDV).
- 4.1.3 We note that no value has been attributed to the existing surface car park. However, the car park has been valued at £1.012 million, therefore if this existing use were to be included in the BLV the surplus would be reduced accordingly.
- 4.1.4 Overall we consider that there is scope for some affordable housing provision within this scheme. The NPPF suggests that affordable housing in BTR schemes should normally be provided in the form of 'affordable private rent' (APR), and the associated guidance suggests that the inclusion of 20% APR in a BTR scheme is a suitable benchmark. Providing 20% of the units (53 units) as APR at 80% of market rent would result in a GDV of £35,158,000 for the flats (thus a total scheme development value of £37,671,400), and a residual value of £3,833,539 which exceeds the stated BLV of £2.96 million by £873,539.
- 4.1.5 As discussed earlier in the report, we consider the premium applied to the BLV to be excessive and suggest a 10% premium, thus a BLV of £2,501,950. This further improves the viability position, showing a surplus of £1,331,589. Therefore, even if the existing use value of the surface car park is taken into account a scheme providing 20% Affordable Private Rent shows a small surplus.
- 4.1.6 In conclusion, we consider that the scheme should be able to support the 20% Affordable Private Rented housing suggested by the NPPF (and meet the draft HBC policy of providing 20% affordable housing on town centre sites). However HBC will have

to consider whether rents at 80% of market rent achieve the desired level of affordability for applicants on their housing register. If not, an alternative quantum or rent level could be agreed).

4.1.7 We need to be clear our review is based on current day costs and values assumptions as described within our review based on the current scheme as submitted. A different scheme may of course be more or less viable – we are only able to review the information provided.

4.1.8 No viability appraisal or review can accurately reflect costs and values until a scheme is built and sold - this is the nature of the viability review process. In this sense, the applicant and their agents are in a similar position to us in estimating positions – it is not an exact science by any means, and we find that opinions will usually vary.

4.1.9 DSP will be happy to advise further as required.

Report Ends
November 2019

Appendix I:
Wellington Way – Retail comparables

Appendix II:
Retail units available for let in WaterlooVille