Hathersage & Besant Court, 104 Newington Green Road

Independent Viability Review

Prepared on behalf of the London Borough of Islington

26th November 2018

Planning reference: P2018/1970/FUL

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Introduction

1.1 We have been instructed by the Planning & Development Division of the London Borough of Islington to undertake a viability review in respect of a proposed redevelopment of Hathersage & Besant Court.

1.2 The applicant is the London Borough of Islington itself. A viability report has been prepared by Deloitte Real Estate on behalf of the applicant. Their report concludes that currently proposed level of affordable housing is the maximum that can reasonably be delivered.

1.3 The Council's Core Strategy Policy CS12 includes a site specific requirement that developments should provide the maximum reasonable level of affordable housing taking into account the 50% strategic target and that, "It is expected that many sites will deliver at least 50% of units as affordable, subject to a financial viability assessment, the availability of public subsidy and individual circumstances on the site". For the Council's own schemes, the target is for 100% of the units to be affordable housing, subject to viability.

1.4 The scheme will provide 45 new-build residential units, and 3 commercial B1/D1 units. The housing will be comprised of 21 private units and 24 affordable units (of which 21 are social rent, and 3 are shared ownership. It therefore exceeds the Council's affordable housing target.

1.5 We have been provided with an Excel-based appraisal of the proposed scheme, together with a breakdown of the build costs. Our Viability Review has scrutinised the cost and value assumptions that have been adopted in the viability assessment, in order to determine whether the current affordable housing offer is the maximum that can reasonably be delivered.

1.6 The Valuation Date for this Viability Review is the date of this report, as stated on the title page. This Viability Review has been undertaken in accordance with the Terms & Conditions provided to the Council and with any associated Letters of Engagement, and should only be viewed by those parties that have been authorised to do so by the Local Authority.

Conclusions & Recommendations

1.7 The applicant has provided an Excel-based appraisal of the scheme. The shows total revenue (GDV) for the scheme at £16.26m. The total build costs are higher, at £22.71m, thus it is shown to generate a negative residual land value of -£6.46m. There is no allowance for developer's profit in the valuation. And the applicant is setting the Benchmark Land Value at nil. Thus £6.46m is the total scheme deficit. These results indicate that additional affordable housing, over and above the level being proposed, cannot viably be delivered.

1.8 Our Cost Consultant, Geoffrey Barnett Associates (GBA), has analysed the applicant's Cost Plan and now concludes that the build costs are broadly reasonable, as detailed in their 16th November addendum report (see **appendix one**). This conclusion was arrived at following detailed discussions with the applicant's cost consultant, in respect of the abnormal costs of the scheme.

1.9 And all of the other cost inputs into the applicant's appraisal appear to be realistic, as we discuss further below.

1.10 The appraisal does not include any allowance for a benchmark land value to the applicant, and does not include any formal developer's profit.

1.11 With respect to appraisal inputs (such as developer profit and benchmark land value), it is standard practice, endorsed by RICS Guidance, that when determining planning applications, the aim should be to reflect industry benchmarks. LPAs should therefore disregard who is the applicant, except in exceptional circumstances (such as personal planning permissions, as planning permissions run with the land). In formulating information and inputs into viability appraisals, these should accordingly disregard either benefits or disbenefits that are unique to the applicant, whether landowner, developer or both. This is the principle (stated in RICS Guidance) that viability assessments for planning purposes should consider the approach of a 'typical', rational landowner, rather than be specific to the applicant in question.

1.12 In this case, a nil benchmark land value is included in the appraisal. This is because the proposed scheme will be a not-for-profit development and the freehold of the site will remain in the Council's ownership. The Council's key objective is to ensure that the scheme is partly self-funding by using capital receipts from sale of the private flats to fund the development of the affordable housing. This objective is clearly different to the primary objective of the traditional private developer which is to maximise profit. We accordingly accept that in this case it is appropriate not to assess viability on the same basis as for a private development.

1.13 Whilst it is standard practice to include such a benchmark land value in appraisals for planning purposes – even in circumstances where the landowner retains the site post-development and has owned the site long-term – given that the Council's primary objective is investment in affordable housing and estate quality generally, rather than generating a land receipt, it is appropriate to include nil land value in the appraisal.

1.14 Unlike typical development appraisals for planning purposes, no formal profit allowance is included in the appraisal. However, there is a “development & administrative allowance” of £453,200 (equal to only 2.7% of the scheme’s GDV) and a contingency equal to 5.4% of the base build costs. This allowance and contingency could be categorised as a “return”; it is common in appraisals of Council schemes for some level of return to be allowed to compensate for the exposure to risk. And the contingency is in some way an allowance for risk. In our experience of Council-led schemes, it is common for some degree of Developer’s Return to be included to compensate for exposure to risk.

1.15 The appraisal includes leaseholder homeloss payments to tenants of two apartments, and compensation payments to two commercial freeholders. We have requested comments from the Council regarding how this figure is calculated, and this has now been provided. The commercial compensation is based on a Council valuation of these freehold assets with an additional allowance added as a further incentive to these freeholders. The valuation approach taken is reasonable.

1.16 With respect to the private housing, we have undertaken our own research and have reviewed the evidence provided by Deloitte, and conclude that the pricing adopted in the applicant’s appraisal is realistic for this development, which will be unlikely to compete at the upper end of the local new-build market.

1.17 The three shared ownership units are values are £445,000-£452,000 and are at the same price as similar-sized private units, therefore it is not clear how these have been valued. The appraisal indicates that a 25% initial equity share will be assumed, and that a rent will be charged on the unsold equity. We are unable to create an accurate valuation of these units without knowing the rent on unsold equity. A typical rent would be 2.5%, and this would typically lead to a capital value at 60% of open market values – as shown by our in-house valuation model. Therefore it appears likely that the values included in the appraisal for these units is overstated (by in the region of £500,000). Regarding the social rent units, we conclude that these have been realistically valued.

Development Costs

1.18 The Bailly Garner Cost Plan includes a contingency of £1,122,000. The total build cost inclusive of this contingency is £18.77m. This is inclusive of design fees, preliminaries, external works and OHP. The build cost is shown as £18.65m in the appraisal, but it is not clear why there is a difference between this and the figure in the Cost Plan. The figure of £18.65m in the appraisal appears to be inclusive of the £1.12m of contingency that is included in the Cost Plan (6.4% of base build cost), thus the £906,400 of contingency shown separately in the appraisal is *in addition* to the Cost Plans' contingency. The contingency of £906,000 in the appraisal is 5% of the Cost Plan cost.

1.19 Our Cost Consultant, Geoffrey Barnett Associates (GBA), has analysed the applicant's Cost Plan and now concludes that the build costs are broadly reasonable, as detailed in their 16th November addendum report (see **appendix one**). This conclusion followed detailed discussions with the applicant's cost consultant, in respect of the abnormal costs of the scheme. And all of the other cost inputs into the applicant's appraisal appear to be realistic, as we discuss further below.

1.20 In addition, there are professional fees of £1,836,100 in the appraisal, which is equal to 10% of the base build cost. There are, however, design fees of £804,844 in the Cost Plan (which is effectively a form of professional fees allowance), thus the combined level of professional fees is substantial and is higher than typical rates. For example, the GLA Toolkit's benchmark rate is 12%; however, in view of the large number of unique buildings being delivered by this scheme, including infill developments in small spaces, there is clearly a high degree of technical difficulty to this scheme which justifies a higher than typical level of fees.

1.21 Finance costs are £147,200 which is a very low level for a scheme of this size. It is calculated based on the Public Works Loan interest rate of 1.50%, which is a suitable approach to adopt.

1.22 All the other cost items, including among others sales fees and marketing fees, are in line with typical benchmark rates.

Commercial units

1.23 The commercial units are 1,345 sq ft, 689 sqft and 1,119 sq ft, all NIA. The rent applied is £32 per sq ft. The rent has been capitalised using a 6.5% yield assuming D1 use, and 5.5% assuming B1. It is not, however, clear which use will actually take this space. It does not appear that any comparable evidence is provided by Deloitte in their valuation report. We have therefore looked at the local market.

1.24 There are available offices at 240b, Kingsland Road, London, E2 8AX available at £30 per sq ft, which is good quality 'post-industrial style' office/studio space, with modern conveniences including air conditioning. This is in close proximity, to the south-east of the subject site and arguably in a marginally superior office location as closer to amenities. Similarly, an office at Stamford Works, Gillett Street is available at £29 per sq ft, and is 'media style' second-hand offices. There are a number of similar premises at around the same rent per sq ft, with the highest we have viewed (within mile radius of subject site) being £32 per sq ft. This indicates that the adopted rents used by Deloitte are reasonable, even allowing for some degree of new-build premium for new office space. Moreover, achieving £35 per sq ft may be challenging for D1 uses, and the level of rents achieved depending on the type of tenants secured – especially as maximising rent may not be the only criteria for securing tenants, as the community benefits these tenants bring will likely be another key consideration.

1.25 Regarding the yield applied by Deloitte, they do not provide any investment sales evidence in support of their estimate. The yield of 6.5% compares to the Knight Frank Investment Guide's figures of 6.0% for 'good secondary' offices, but the subject site's location is arguably slightly below 'good secondary' quality, given its distance from major office hubs like the City and Docklands, and its distance from good local amenities. In this context, 6.5% is a realistic estimate.

Private residential values

1.26 The housing will be comprised of 21 private units and 24 affordable units (of which 21 are social rent, and 3 are shared ownership. The private housing has been attributed an overall value of £729 per sq ft by Deloitte. This is an infill development within the existing Hathersage Court/Besant Court estate. It will therefore retain some of its Estate character which may be perceived negatively from the point of view of private purchasers. There will be seven new blocks in total. These include a block which will partly overlook Newington Green park, which may bolster prices.

1.27 Deloitte's August 2018 report states that this estimate is based on discussions with local agents. We have considered in detail the following nearby comparable schemes:

- <u>Essence, 10-14 Crossway, Stoke Newington, N16</u> – this is to the east of the site, and close to Kingsland High Street. Heatmap data suggest that this location is broadly similar to the subject site's location in terms of residential prices. The achieved pricing ranges from £717-£933 per sq ft depending on unit type, with the one-beds having the highest prices. The two-beds achieved £599,000-£630,000. By comparison, the proposed two-beds which we calculate average £626,000 (£725 per sq ft). Whilst we consider Essence to be in a marginally superior location to the proposed scheme given the latter is an infill development within an estate, the proposed two-beds are generally larger than these Essence units thus similar overall pricing can be expected.

- <u>FiftySevenEast, Dalston, E8</u> – This scheme is on Kingsland High Street, very close to the Essence scheme discussed above. It is difficult to make a close comparison with the proposed scheme, given the different setting. Other than some exceptionally high prices, most of the sales are below £850 per sq ft at this comparable scheme. The achieved prices are considerably higher (£699,000 up to £1.19m) for two-beds than those in the Hathersage scheme. It is not clear why some of the prices at this development are considerably higher than the nearby Essence development. But the lower prices achieved are more in line with Essence.

1.28 The below table of comparable sales in the local area indicates that the pricing adopted for the proposed units is generally higher than locally achieved prices for re-sale (i.e. not new-build) houses. The exceptions are typically superior properties, such as 64b Ferntower Road (sold of £825,000) which is in an attractive road of period properties – very close to the subject site.

Table One: Sales within ¼ mile of Hathersage site, within last six months

Address	Last sale price	Last sale date	Property type	Year built	Bedrooms
Flat B 97 Newington Green Road N1 4QX	£625,000	20 Apr 2018	Flat	1890	1
Flat B 30 Petherton Road N5 2RE	£484,000	27 Apr 2018	Flat	1880	1
Flat C 93 Newington Green Road N1 4QX	£340,000	27 Apr 2018	Flat	1900	1
64b Ferntower Road N5 2JH	£840,000	20 Jun 2018	Flat	1890	1
Flat C 12 Pyrland Road N5 2JD	£580,000	08-Jun-18	Flat		2
82 Mildmay Avenue N1 4FE	£575,000	13 Jul 2018	Flat	2013	2
Flat 7 Newington Green N16 9BT	£515,000	30 Jul 2018	Flat	1890	2
43 Mildmay Avenue N1 4FD	£272,500	16 Jul 2018	Flat		2
22 Heaven Tree Close N1 2PW	£1,135,000	16 Apr 2018	Terrace	2002	3
29 Wolsey Road N1 4QG	£812,500	19 Jul 2018	Flat		3
Flat A 26 Beresford Road N5 2HZ	£965,000	13 Aug 2018	Flat	2005	4
Flat 2-5 12 Mildmay Grove South N1 4RL	£403,000	03-Aug-18	Flat		
51 Ferntower Road N5 2JE	£347,000	08-Jun-18	Flat		

1.29 We have undertaken our own research into new-build local market, and have compiled the following average values per sqft from the comparable schemes:

The Harper Building	£880 psf asking
Woodberry Down (Phase 2)	£885 psf asking
Aqua	£765 psf asking
Artisan	£710 psf asking
20Four	£900 psf asking
XY Apartments	£950 psf achieved
321 Holloway Road	£715 psf asking
Queensland Terrace	£800 achieved in latest phase
400 Caledonian Road	£740 psf asking
Rear of Odeon Cinema	£850 psf asking

1.30 For a scheme at Grenville Road we were involved in a viability assessment in which private values were estimated at £727 per sq ft by Montagu Evans, in their January 2017 report. Since then, prices have increased by 3.4% in Islington according to the Land Registry House Price Index (HPI) up to July 2018 which is the latest month for which data is available. This would give £752 per sqft. This is a substantially distance from the subject site, but a broadly similar market in terms of being a more peripheral, lower-valued part of the Borough.

Social Rent – capital values

1.31 The Social Rent units have been attributed a capital value of £2.43m. This has been arrived at by applied the Council's Social Rent level of £125.04 up to £177.88 per week. We assume that their rents are inclusive of service charge. A multiplier of 15 is then applied to this, with no further allowances being made for management & maintenance costs, rent inflation, voids, or any other items. This is exactly same approach as has been used in previous appraisal including for the recent Elthorne Estate redevelopment. In that case, we created a more conventional affordable housing valuation using our own bespoke model; this included standard assumptions used in Registered Providers' valuations, including a yield of 6%, 15% management & maintenance, and 2% inflation on on-costs and rent. The difference in capital value was small and within the margin of error for affordable housing valuations, and this same conclusion applies to the Hathersage & Besant valuation given that exactly the same valuation assumptions have been used.

Shared ownership – capital values

1.32 The three shared ownership units are values are £445,000-£452,000 and are at the same price as similar-sized private units, but it is unclear why this has been done as it would be typical for lower capital value to apply to shared ownership units than private units. The appraisal indicates that a 25% initial equity share will be assumed, and that a rent will be charged on the unsold equity, but these assumptions do not appear to have been applied in the valuation. We are unable to create an accurate valuation of these units without knowing the rent on unsold equity. A typical rent would be 2.5%, and this would typically lead to a capital value at 60% of open market values – as shown by our in-house valuation model. Therefore it appears likely that the values included in the appraisal for these units is overstated (by in the region of £500,000).

Appendix One

Geoffrey Barnett Associates

ADDENDUM REPORT OF THE COST PLAN
PREPARED BY
BAILY GARNER

FOR

HATHERSAGE AND BESANT COURT, ISLINGTON

16 November 2018

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APPENDICES:

1.0 REVIEW & COMMENTARY:

1.1 Our initial report was issued on 16th October 2018, and our calculation at that time was that costs were 13.80% higher than expectation.

1.2 At that time cost information provided was relatively limited. We have subsequently been provided with further information in the form of a cost plan.

1.3 We have studied the further information that had been provided. The additional information included quantified breakdown of costs showing additional abnormals influencing costs.

1.4 We have reviewed Sections 9.3, 9.4, 9.7, 9.8. and 9.9 of the cost plan to ascertain whether we consider any further abnormal costs not covered by BCIS rates could be relevant, with the following conclusions – see Appendix E:

- Large area of zinc cladding to walls. We have allowed additional £150/m2
- Sedum roof and roof terraces. We have allowed additional £50/m2
- Aluminium composite windows. We have allowed additional £100/m2
- Piling foundations. We have allowed additional £100/m2
- Basement. We have allowed extra over £1000/m2 applied to the area of the basement only.

1.5 On the basis of the foregoing we have calculated a total construction cost of £18,325,626– see Appendix E.

1.6 The difference between costs in the cost plan and our assessment of costs is £444,374 or 2.37 % - see Appendix F.

CONCLUSION:

2.0 2.1 We assume the difference between costs in the cost plan and our assessment of costs can be explained by the council’s procurement methods (which we understand is via framework agreement). On this ground we conclude the construction costs put forward in the cost plan are within acceptable estimating margins of our own assessment of costs.

APPENDIX A

CALCULATION OF COSTS USING BCIS M2 RATES

Residential - 4-5 storeys (Block A and B)	2,637	m2 @	£2,045 /m2	£5,392,665
Residential - 6 storeys (Block C)	581	m2 @	£2,391 /m2	£1,389,171
Residential - 2 storeys houses (Block D and E)	401	m2 @	£1,913 /m2	£767,113
Residential - 4 storeys (Block F)	384	m2 @	£2,045 /m2	£785,280
Substation - Block G	15	m2 @	£2,980 /m2	£44,700
Commercial - Block H	114	m2 @	£2,612 /m2	£297,768
Residential - 1 storey, cycle store (Block J)	68	m2 @	£1,727 /m2	£117,436
Residential - 4-5 storeys (Block K)	612	m2 @	£2,045 /m2	£1,251,540
Commercial - (Block K)	254	m2 @	£2,612 /m2	£663,448
				£10,709,121

<u>Additional and abnormal costs</u>

Facilitating works (site clearance)		£220,000
Work to existing buildings		£228,199
External works		£2,159,954
Preliminaries on additional costs	19.30%	£503,374
Overheads and profits on additional costs	5%	£155,576
Design fees	5%	£698,811
Site abnormals: due to location of new and existing buildings the site will be run as a number of construction sites	5%	£733,752
Risk	5%	£770,439
		£16,179,226

Notes:
1. BCIS rates are Upper Quartiles rates, rebased to Islington and current date (3Q2018)
2. Additional and abnormal costs are generally taken from the cost plan.

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APPENDIX B

ADJUSTMENT OF COST PLAN TO REFLECT CURRENT DATE

Cost from cost plan	£18,770,000
Date basis of cost plan	3Q2018
Current date basis	3Q2018
BCIS TPI at date of cost plan	313
BCIS TPI at current date	313
Cost at current date	**£18,770,000**

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APPENDIX C

COMPARISON OF DATE-ADJUSTED COST PLAN AGAINST COSTS USING BCIS M2 RATES

Cost using BCIS m2 rates - Appendix A	£16,179,226
Cost from cost plan (adjusted to current date) - Appendix B	£18,770,000
Difference £	£2,590,774
Difference %	13.80%

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APPENDIX D

COMPARISON OF ELEMENTAL M2 RATES

		Cost plan			BCIS	Difference
		£ nett	£ inc prelims & OHP	£/m2	£ /m2	£/m2
1.1	Substructure	1,087,397	1,430,234	282	189	-93
2.1	RC frame	714,729	940,071	186	205	19
2.2	Upper floors	16,636	21,881	4	113	108
2.3	Roof	626,608	824,167	163	121	-41
2.4	Stairs	318,383	418,764	83	37	-45
2.5	External walls	2,112,680	2,778,771	549	246	-303
2.6	Windows and external doors	869,435	1,143,553	226	117	-109
2.7	Internal walls & partitions	332,903	437,861	86	97	10
2.8	Internal doors	386,961	508,963	100	64	-37
3.1	Wall finishes	397,228	522,467	103	99	-4
3.2	Floor finishes	580,288	763,243	151	85	-66
3.3	Ceiling finishes	205,820	270,711	53	52	-1
4.1	Fixtures & fittings	528,705	695,396	137	82	-56
5.1	Sanitaryware	189,269	248,942	49	39	-10
5.3	Disposal installations	30,103	39,594	8	17	9
5.4	Water installations	321,372	422,695	83	43	-41
5.5	Heat source	122,620	161,280	32	44	13
5.6	Space heating	229,724	302,152	60	148	88
5.7	Ventilatiopn Systems	108,818	143,126	28	24	-4
5.8	Electrical	450,844	592,987	117	114	-4
5.9	Gas installations	23,522	30,938	6	9	3
5.10	Lifts	316,100	415,761	82	50	-32
5.11	Protective installations	305,753	402,152	79	15	-64
5.12	Fire alarms, comms and security	150,027	197,328	39	21	-18
5.13	Special installations	326,723	429,733	85	68	-17
5.14	BWIC	60,893	80,091	16	16	0
		10,813,541	**14,222,861**	**2,808**	**2,114**	-694

Notes:

1. BCIS rates are Upper Quartiles rates, rebased to Islington and current date (3Q2018)

APPENDIX E

GBA ASSESSMENT OF COSTS

Cost using BCIS rates (from Appendix A)		16,179,226
Additional and abnormal costs		
1	Zinc cladding to external walls £150/m2 @ 5,066m2	759,900
2	Extra over for Sedum roof and roof terraces £50/m2 @ 5,066m2	253,300
3	Aluminium composite windows £100/m2 @ 5,066m2	506,600
4	Extra over for basement £1000/m2 @ 120m2	120,000
5	Piling foundations £100/m2 @ 5,066m2	506,600
		£18,325,626

APPENDIX F

COMPARISON OF DATE-ADJUSTED COST PLAN AGAINST GBA ASSESSMENT

GBA assessment of costs - Appendix E	£18,325,626
Cost from cost plan (adjusted to current date) - Appendix B	£18,770,000
Difference £	£444,374
Difference %	2.37%