Private and Confidential

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Our Reference: [redacted]
Your Reference: 17/02443/OUT

[redacted]

Date : 14th September 2018

Dear Simon,

DESK TOP REVIEW OF DEVELOPMENT VIABILITY ASSESSMENT
PROPOSED SCHEME: 2 Victor Street, Southampton. SO15 5LH

I refer to our fee quote dated 13th December 2017 and your email dated 30th July 2018 confirming your formal instructions to carry out a desk top viability assessment in respect of the above proposed development.

This report is not a formal valuation.

The date of assessment is 14th September 2018.

We have reviewed the assessment provided by Max Holmes on behalf of the applicant Mr S Reeves.

The assessment has been made by comparing the residual value of the proposed scheme with an appropriate benchmark figure having regarding to the National Planning Policy Framework and the published RICS Guidance Note into Financial Viability in Planning.

The principal objective of our Brief and the subject of this report are to establish whether there is financial justification for any affordable housing and section 106 contributions.

General Information

It is confirmed that the viability assessment has been carried out by [redacted], acting in the capacity of an external valuer, who has the appropriate knowledge and skills and understanding necessary to undertake the valuation competently, and is in a position to provide an objective and unbiased valuation.

Checks have been undertaken in accordance with the requirements of the RICS standards and have revealed no conflict of interest. DVS has had no other previous material involvement with the property.

The client will neither make available to any third party or reproduce the whole or any part of the report, nor make reference to it, in any publication without our prior written approval of the form and context in which such disclosure may be made.

You may wish to consider whether this report contains Exempt Information within the terms of paragraph 9 of Schedule 12A to the Local Government Act 1972 (section 1 and Part 1 of Schedule 1 to the Local Government (Access to Information Act 1985) as amended by the Local Government (access to Information) (Variation) Order 2006.

Our assessment is provided for your benefit alone and solely for the purposes of the instruction to which it relates. Our assessment may not, without our specific written consent, be used or relied upon by any third party, even if that third party pays all or part of our fees, directly or indirectly, or is permitted to see a copy of our valuation report. If we do provide written consent to a third party relying on our valuation, any such third party is deemed to have accepted the terms of our engagement.

None of our employees individually has a contract with you or owes you a duty of care or personal responsibility. You agree that you will not bring any claim against any such individuals personally in connection with our services.

This report remains valid for 3 (three) months from its date unless market circumstances change or further or better information comes to light, which would cause me to revise my opinion.

Following the referendum held on 23 June 2016 concerning the UK's membership of the EU, the impact to date on the many factors that historically have acted as drivers of the property investment and letting markets has generally been muted in most sectors and localities. The outlook nevertheless remains cautious for market activity over the coming months as work proceeds on negotiating detailed arrangements for EU exit and sudden fluctuations in value remaining possible. We would therefore recommend that any valuation is kept under regular review.

Background:

The subject site extends to approximately 0.15 Ha (0.37 Ac) and comprises a single detached building, formerly used as a working men's club but is now fitted out and occupied as a children's soft play centre with bar area. There is also an existing 3 bedroom residential flat here and the total combined floor area of the existing building has an estimated gross internal area (GIA) of 1,290m2.

The site sits on the corner junction of Victor Street and Crown Street with a large Sainsbury's supermarket directly to the south-west, and a primary school to the north. The site adjoins the site of an historic church on the south-east side which is currently occupied by the Salvation Army.

The current planning application for the site is as follows:

'Erection of part 5, part 6 storey building to contain 45 flats with associated car parking, stores and external works'

The applicant is stating that following their assessment the scheme with no affordable housing and £117,261 of CIL contributions and £21,000 of S.106 contributions shows a profit of 7% on gross development value and therefore no affordable units are viable.

The Scheme:

We have been provided with the assessment undertaken on behalf of the applicant.

For the purpose of this desk top assessment we assume the areas provided by the applicant are correct and have assumed that 16 units as affordable would be policy compliant.

The scheme as proposed by the applicant is as follows:

Type	Number of Units	Average Unit Size Sq m	Total Net Sq m
Private Residential			
One bedroom apartment	34	49.97	1,699
Two bedroom apartment	6	67.83	407
Three bedroom apartment	5	87.0	435
Total	**45**		**2,541**

In addition, the scheme will provide;

- 7 car parking spaces in total.
- Cycle and refuse storage facilities.

The gross internal area (GIA) for the proposed block is indicated at 3,429m2 which equates to a net – gross ratio of approximately 74.1% which is towards the lower end of the range we would expect for this type of development.

However, the total area includes cycle and refuse stores which account for approximately 80m2 – 100m2, and the building also has a lift so overall the net-gross ratio is deemed to be within an acceptable range.

Viability Assessment:

This report deals with each major input into the viability assessment of the scheme. This desk top assessment has been undertaken following our own research into both current sales values and current costs. We have used figures put forward by the applicant if we believe them to be reasonable.

We have used a bespoke excel based toolkit with cash flow to assess the scheme which is attached as Appendix 1.

We would summarise our assessment of the Scheme as follows:

1) Development Value -

a) Private Residential / Commercial:

The applicant has adopted the following open market sales values compared to ours:

Type	Applicant (Average Value)	DVS (Average Value)
1 bed apartment	**£130,000**	**£140,000**
2 bed apartment	**£150,000**	**£160,000**
3 bed apartment	£180,000	£180,000

At this stage no comparable sales evidence has been provided to us by the applicant's representative to substantiate their submitted figures.

Within their written report they have commented that similar existing properties in this location are currently achieving re-sale values of £130,000, £150,000 and £180,000 respectively.

They then comment that they would hope a premium could be achieved for the subject units, but have not uplifted the values to reflect this.

From our own research we agree that a new-build premium could be achieved here and as a result consider that the 1 and 2 bedroom units could achieve slightly higher values as set out in the table above. The 3 bedroom values at £180,000 are in line with our revised values for the 1 and 2 bedroom units.

The values here are restricted to an extent by the lack of car parking and our revised figures take into account the fact that an additional £10,000 would need to be added to reflect a parking space.

b) Ground rents:

For a development of this type we would expect the residential units to be sold on a long leasehold basis with both a ground rent and service charge payable. The ground rents would have a value.

The developer has indicated a freehold value of £120,000 which equates to an average of approximately to £133.33 per unit per annum capitalised using a 5% yield.

This may be considered to be on the low side when comparing to general ground rental incomes, but from our research, ground rental incomes in this location appear to be lower than average. Therefore we have accepted the submitted freeholds value as reasonable and included the same in our appraisal.

It should be noted that the Government are currently proposing legislation to limit ground rental income. If this were to happen then it may cause us to revise our revenue figures to potentially reflect the ground rent income in the capital values.

c) Car Parking:

The applicant has included an additional £70,000 to account for the 7 car parking spaces. We have not been informed whether these spaces will be allocated to any particular units, and they may be available to be purchased in conjunction with the individual flats.

£10,000 per space is deemed an acceptable level of value for this taking account of the density of development in this location, close proximity to local shops (including large Sainsbury's supermarket), and close proximity to a main bus route.

d) Gross Development Value (GDV):

On the basis of the proposed scheme, with no affordable housing, we assess the gross development value to be in the region of **£6,810,000** whilst the applicant has adopted a total of **£6,410,000** - some £400,000 lower.

2) Development Costs -

a) Build Cost:

The applicant has assessed the overall base build costs at £4,600,000 on the basis of approximately £1,341 per m2 which is assumed to include a build contingency. We have taken account of the BCIS rates for building these types of properties and have adjusted for location.

On this basis we consider the base build costs to be reasonable as the construction rate sits between current Lower Quartile and Median figures for a 3-5 storey block which is what we would expect to see in this lower value location.

The proposed block will be part 6 storey and it is worth noting that the BCIS guide figures increase dramatically for a 6 storey+ block.

In addition, £50,000 has been included for a landscaped decking area for car parking and amenity which is also deemed reasonable for this scheme and will essentially cover the costs of all landscaping and external works required. Whilst this will be minimal due to the site coverage of the new building, there will still be associated costs to be accounted for.

b) Build Contingency – The applicant has not included a separate contingency for the proposed scheme but we assume that this is reflected in the overall base build costs of £4,600,000 as detailed above. We would usually expect to see 3 - 5% of base build costs allocated for build contingency.

c) Professional Fees – The applicant has included £200,000 for professional fees plus up to £40,790 for planning costs. This equates to approximately 5.18% of base construction costs in total. Whilst this is lower than we would usually expect to see, we have accepted it as reasonable for this scheme and included the same in our appraisal for the purposes of viability testing.

d) Abnormal costs – The applicant has included the following abnormal costs:

- Service connections - £138,000 (£3,000 per unit plus 1 additional for the freehold supply)
- NHBC warranties - £31,500 (£700 per unit)
- Pavement closures - £3,000
- PV Panels - £25,000 (£555.55 per unit)
- Demolition costs - £25,000

These costs are considered to be reasonable, if slightly conservative with regard to the NHBC warranties and PV panels, but we have included the same within our appraisal for the purposes of our assessment.

e) Section 106/CIL Costs – The applicant has included £117,261 for CIL contributions taking account of the existing building's floor space. They have also included a total of £21,000 for S.106 contributions which are believed to be estimated figures.

However, you have informed us that the total required CIL will be £214,241 and S.106 will be £69,102 and we have therefore included these figures in our appraisal instead but if this differs then it will affect our assessment**.**

f) **Sales and Marketing Fees –** The applicant has included a sales and marketing fee of 1.25% of the GDV which is also intended to cover all legal sales costs and the cost of creating a show flat for each type.

This allowance is lower than we would expect when compared with other similar schemes we have assessed and therefore do not consider it to be overstated and have included the same within our appraisal for the purposes of viability testing.

g) **Finance costs -** The applicant has adopted a finance rate of 7% which is in line with similar schemes that we have previously assessed. However, it should be noted that the applicant has based their borrowing on 50% of GDV over 30 months but for the purposes of viability testing our appraisals are constructed on the assumption of 100% debt finance.

Our total finance costs are therefore **£364,797** which is significantly higher than those estimated by the applicant at **£59,000**.

h) **Developers Profit –** The applicant has indicated that the scheme will produce a profit level of approximately 7% on GDV but has not stated what they would usually expect from such a scheme.

For residential schemes of this type we would normally adopt a profit level of between 15% - 20% and have therefore carried out an assessment based on a 17.5% profit level.

i) **Development Programme –** The applicant has not provided a detailed timeframe for the scheme but has indicated a total scheme length of 30 months which does not appear unreasonable. We have assumed the following programme:

- Build Period of 12 months following a 6 month lead-in period.
- Pre-sales of 15 units after practical completion followed by a sales period of 9 months for the remaining units beginning directly after the build period of 12 months.

Land Value – Following various appeal cases, NPPF, and RICS guidance it is well established that viability assessments are carried out in order to calculate the residual land value that the scheme can afford which is then compared to the benchmark value of the site.

The revised NPPF suggests that the Benchmark Land Value should be established on the basis of Existing Use Value (EUV), plus a premium for the landowner. However, Alternative Use Values can be taken into account where there is an existing implementable permission for that use. In these cases a premium is not added.

The applicant has assessed the EUV of the site at **£600,000** based on a current rent passing of £70,000. A capital value of £600,000 equates to a capitalisation yield of approximately 11.4%.

We have not been provided with any details of any current lease or agreement in place and have no record of this rent on our office records.

Due to the nature of the current use (children's soft play centre), the general age and condition of the building, and the fact that it is earmarked for redevelopment, it is assumed that any lease that is in place will be on a short term, or that there is a different sort of agreement in place which provides greater flexibility for both landlord and tenant.

We do however hold records from August 2013 which show that the applicant acquired the property/site on the open market for £300,000 at that time. Whilst there may have been some movement in the general market for this type of property it is not considered to be significant due to the age and nature of the existing building and therefore the acquisition price is deemed to be a more accurate reflection of the current EUV in light of lack of rental detail and current evidence.

The NPPF guidance refers to a seller incentive of between 15% and 20% on top of the EUV. It is not known whether the property has been internally refurbished or improved at all since it was acquired but if this is the case then this may have enhanced the value slightly. In light of this uncertainty and the time delay since the acquisition we consider a 20% seller incentive to be justified in this instance.

Therefore we have included a benchmark land value of **£360,000** in our appraisal for the purpose of viability testing.

In addition we have allowed for stamp duty at the current rate and agent/legal fees in our appraisal.

Overall assessment:

Following our desktop assessment we are of the opinion that the proposed scheme, with no affordable housing but with £214,241 of CIL contributions, £69,102 of S.106 contributions and a developer profit of 17.5% is not viable and that no surplus would be available towards an affordable housing contribution. Our appraisal shows a deficit figure of -£619,130 (see Appendix 1.)

Whilst we have agreed with a lot of the applicant's submitted figures, some of their costs are below industry standard levels for this type of development.

The differences between ours and the applicant's figures are as follows:

- GDV (1 and 2 bedroom units only)
- Finance costs (we are higher due to the reasons detailed in section 2.g above)
- Benchmark land value

It should be noted that the applicant's viability submission is of poor quality and does not contain any reasoned evidence to substantiate their adopted figures. In addition, they have not used a development appraisal toolkit to present their results.

In order to provide the Council with an idea of the viability of the proposed scheme, we have carried out our own research of market values in this location, and of current construction costs adjusted for this location. We have accepted the applicant's submitted costs where they do not appear to be overstated for the proposed scheme.

Our appraisal shows that the proposed scheme will achieve a profit level of approximately 8.4% on GDV which, in the current economic climate, would mean that debt finance may not be able to be secured and brings into question the deliverability of the proposed scheme. It should be noted that the applicant anticipates a profit level of just 7% on GDV.

In order for the scheme to be deliverable we consider that a minimum profit level of 15% on GDV should be achieved which, in this case would mean increasing the anticipated revenue by at least an additional £400,000. From our research on sales evidence, there are no recent sales and nothing currently on the market which would suggest this is achievable at the present time.

I trust this report deals with the issues as required but please do not hesitate to contact me if you have any queries and I would welcome the opportunity of discussing this with you in greater detail.

Yours sincerely

[redacted]

Reviewed by:

[redacted]

Appendix 1 – 100% Open Market Viability Appraisal

Appendix 1

Viability Appraisal