

Viability Report

**Heygate Estate
Regeneration Scheme
Elephant and Castle
London
SE17**

London Borough of Southwark

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1. INTRODUCTION

I refer to your instructions dated 10th October 2011 and my letter of confirmation dated 10th October 2011 with our Standard Terms of Business requesting my valuation advice in relation to the various regeneration schemes at Elephant and Castle as described below.

National Planning Policy Framework states *"To ensure viability, the costs of any requirement likely to be applied to development, such as requirements for affordable housing, standards, infrastructure contributions or other requirements should, when taking into account of the normal cost of development and mitigation, provide competitive returns to a willing land owner and willing developer to enable the development to be deliverable"*

(National Planning Policy Framework, 2012, paragraph 173)

In order for this to be demonstrated, the applicant needs to provide a viability study that shows why a policy compliant scheme would render the development unviable. This study needs to be sufficiently detailed with evidence supporting the key inputs into the study.

From your brief I note you require a review of the viability study submitted by Savills as part of the planning application on behalf of Lend Lease for development at the Heygate Estate to inform assessment of the acceptability of the scheme with regard to the applicant's proposed affordable housing and other s106 planning obligations.

My role therefore is to provide a report to you in which I will review the report provided by the applicant and undertake:

a) Market research of markets conditions and all other key elements affecting viability including:

- Sales rates for private residential, affordable housing and commercial
- Land Values
- Build costs
- Fees
- Profit levels
- Finance

In addition we would consider predictions on future prospects by.

- b) Applying the market evidence and all other information including build and Infrastructure costs within the Financial Model provided by the applicant (Due to the complexity of the model, DVS have not created a separate model in this instance and have worked with the applicant's bespoke spreadsheet).
- c) Undertake sensitivity analysis on ranges of different market conditions/ scenarios for each assessment.
- d) Reporting to you confirming the methodology used and assumptions made, our findings and their implications together with our conclusions.

The key policy considerations are the Council has an affordable housing requirement of 35% and the rented accommodation should be based on target rents.

2. LOCATION AND PROPOSALS

The Site is located in Elephant and Castle, within the London Borough of Southwark (LBS) and has an SE17 postcode. The Site is bound by New Kent Road (A201) to the north; Rodney Place and Rodney Road to the east; Wansey Street to the south; and Walworth Road (A215) and Elephant Road to the west. Heygate Street bisects the Site with junctions to Walworth Road to the west and Rodney Place and Rodney Road to the east.

The site has good transport links as it is close to Elephant & Castle tube station which is on the London Underground system and is located on the boundary of Travelcard Zone 1 and 2. The station is on the Bank branch of the Northern Line between Kennington and Borough, and is the southern terminus of the Bakerloo Line, the next station being Lambeth North in addition there is also the railway station, which is managed by First Capital Connect, with services operated by both First Capital Connect Thameslink and Southeastern. The area is also served by numerous bus routes.

The Heygate Site represents a significant regeneration opportunity for Southwark within the Elephant and Castle Opportunity Area.

Site Description

The Site is predominantly occupied by the Heygate Estate, owned by Southwark; this is a 1970s housing estate, there are 1,107 residential units within the application boundary, located within several buildings of up to 12 storeys in height. I understand that the Estate is largely vacant with less than a hand full of units occupied.

The Site extends to 9.71 hectares (23.98 acres).

I have been provided with the following breakdown of the existing Heygate Estate residential stock that is contained within the red line plan:

BUILDING	UNITS					TOTAL
	Bedsits	1 bed	2 bed	3 bed	4 bed	
Kingshill	0	119	109	0	0	228
Wansey Street	0	0	4	15	0	19
Swanbourne	0	88	22	0	0	110
Ashenden	0	198	44	0	0	242
Claydon	0	106	110	0	0	216
Marston	0	56	48	0	0	104
Cuddington	0	0	19	39	22	80
Chearsley	0	0	21	34	17	72
Risborough	0	0	10	16	10	36
TOTAL	0	567	387	104	49	1,107
% of stock	0%	51%	35%	9%	4%	100%

In addition to the Heygate Estate, the Site incorporates a number of other land uses, and areas of open space. These include, garages located beneath the residential units, pedestrian walkways, playgrounds and sports areas, gardens, including a number of trees and the Elephant Road Park, a former petrol station (located to the southwest of the Site), a boiler house, a small number of retail units and community facilities; and Crossway Church on New Kent Road.

The Surrounding Area

The land uses surrounding the Site are primarily residential, with residential land uses to the north, south, and southwest, including the Draper, Newington and Alberta Housing Estates to the southwest; Nelson and Browning Estates to the south; and Rockingham Estate to the north. Residential properties on Wansey Street and Brandon Street are located directly opposite the Site to the south.

Student accommodation is located to the southwest and north of the Site, and the mixed use 44 storey Strata Tower is located to the southwest. There are a number of other land uses, together with significant transport infrastructure, that are also located within the vicinity of the Site.

The Elephant and Castle Shopping Centre is to the west of the site, comprising a supermarket and other retail units; a bowling alley, Bingo Hall, a public house, the Coronet Theatre, cafes, restaurants and hot food takeaways there is also an external market space.

3. PROPOSED SCHEME

The proposed development comprises an outline planning application for the demolition of all structures on the Site and its redevelopment for a mix of uses. Accordingly, planning permission is being sought for the following development:

"Demolition of all existing structures and bridges and redevelopment to provide a mixed use development comprising residential (C3), retail (A1-A5), commercial (B1), leisure and community (D1 and D2), and energy centre (sui generis uses), new landscaping, park and public realm, car parking, means of access, and other associated works."

The proposed scheme is to be developed over approximately a 13 year development timeline.

The Development proposes a mix of uses, in summary; the application seeks permission for a maximum total of 330,741 sqm GEA floorspace. Table 2 below defines the maximum and minimum floorspace figures for each category of land use proposed.

Land Use	Use Class	Minimum GEA (m ²)	Maximum GEA (m ²)
Residential	C3	160,579	254,400
Retail	A1/A2/A3/A4/A5	10,000	16,750
Business	B1	2,000	5,000
Community and Culture	D1	1,000	5,000
Leisure	D2	1,000	5,000
Sui Generis / Energy Centre	Sui Generis	500	925
Sub -Total		175,079	287,075
Parking;		34,854	43,666
Servicing; Plant; Storage			
TOTAL		209,933	330,741

The application seeks permission for a maximum level of residential floorspace of 254,400 m² (GEA) and a minimum level of 160,579 m² (GEA). This will be distributed across the development and can accommodate between 2,300 and 2,462 units depending on the precise mix and unit sizes.

The Site is sub-divided into five areas these are: The Park; Walworth Road; New Kent Road; Walworth Local; and Rodney Neighbourhood.

The Site is further sub-divided into 12 individual development plots (H1-H7, H10, H11a, H11b, H12, and H13) plus a park pavilion (PAV1). The individual development plots contain a mix of residential and other lands uses, and are of varying heights and sizes according to the character area in which they are located.

In addition to the built floorspace set out above, the development includes areas of open space, including a new park, gateway spaces, and new streets. The development will provide a minimum of 45,286 sqm (4.53ha) of areas accessible to the public.

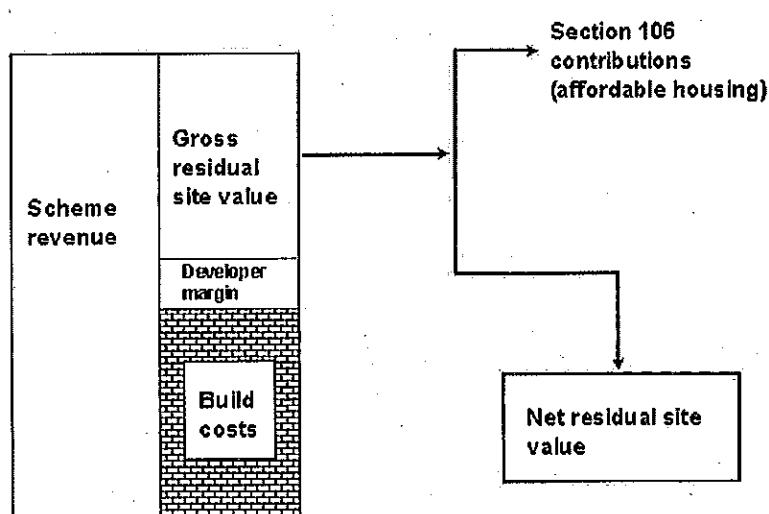
The development will provide a maximum of 616 car parking spaces and a maximum of 3,136 cycle parking spaces.

4. VIABILITY METHODOLOGY:

General viability approach

The recommended approach to undertaking development assessments is provided in a number of guides. These include the National Planning Policy Framework, RICS VIP 12- "Valuation of development land", RICS GN "Financial Viability in Planning", and the GLA Three Dragons Guide (2011).

The approach recommended is to assess viability based on a residual valuation basis. This means assessing the development value of the scheme and deducting from this the costs of the development to leave a gross residual sum representing the site value and planning policy requirements. The following table illustrates this:



This residual site value is then compared to a Benchmark site value. This is based on Market Value, and assumes that the value has regard to development plan policies and all other material planning considerations and disregards that which is contrary to the development plan. This Benchmark site value takes in to account the value of the existing use of the property, appropriate alternative uses and a competitive return for the landowner.

If the residual site value is in excess of the Benchmark site value the scheme is viable and should be planning policy compliant. If it falls below the Benchmark site value it may not be viable, and may require a reduction in delivery of planning policy requirements.

The GLA Three Dragons Guidance Note (2011) considers the issue of adopting the actual price paid as a Benchmark site value. The GN states (P9):

"Under all circumstances, it is important to stress that the amount actually paid for the site should be considered contextual/comparative information only when negotiating schemes. The result from the Toolkit should determine whether a fair price has been paid for land reflecting policy, location, development mix and density."

Residual valuation toolkit

The usual way of carrying out a residual valuation is to use a toolkit. The GLA recommend that in London a purpose designed model "Three Dragons" is used. This toolkit is updated on a regular basis with guide data.

The benefit of using this toolkit is that it works out a residual value to compare against the benchmark site value and shows whether the scheme is viable or not if making assumptions on the developer's profit. (ie Developer return, internal overheads and contractor's return on affordable housing.) Therefore, whilst it has a number of shortcomings, it does assist in understanding if a scheme is viable.

Whilst the Three Dragons toolkit is widely used, it does not carry out the accurate assessment of interest and funding costs, taking in to account the holding cost of the site value. This can be an important element in a valuation and needs to be properly considered. To deal with this, valuers generally carry out a residual valuation on another residual valuation toolkit, inputting the benchmark site value as an assumed input. This then works out what the interest costs would be on this basis. The interest cost from this model can then be compared to the calculations in the Three Dragons toolkit and any adjustment required can be manually input.

I have reviewed the viability of the application scheme based on the assessments carried out by Savills and due to the complexity of the scheme the Three Dragons Tool kit is not suitable or capable of handling a scheme of this nature. The applicant has provided a bespoke financial model which is created in an Excel Spreadsheet. The model is not a residual land value based model, it uses a fixed land price and provides an analysis of the profit that the scheme will generate.

The usual approach to a viability study is a current value and current cost basis; however, it is unrealistic to think that a scheme of this nature can be viable on a day one basis, particularly in the current climate and duration of the development.

The proposal involves a multi stage development with considerable infrastructure requirements early in the programme, in order to maximise savings it is not unrealistic for

infrastructure to be implemented for future stages at an early point in the programme but this will affect the initial viability of the scheme.

The period of time we are considering is approximately ten years from commencement and this may well stretch depending upon market conditions.

In undertaking a current cost approach it also difficult to reflect the regeneration effect that the development will have, which will potentially enhance values as the scheme becomes more established.

The applicant has provided a financial model which allows for escalation of both costs and values, having regard to supporting documents produced by other consultants.

Savills have adopted a [REDACTED] profit on cost approach and identified a significant gap between that and what the escalated model currently shows, they are looking to close this gap by various approaches including the enhancement of the affordable housing value through tenure changes.

I think it is unrealistic to look at profit on cost basis for a development of this type, an IRR approach would be more appropriate; however, this makes it difficult to analyse any potential gap that may exist, essentially this requires various scenarios to be run.

The IRR approach is not a common method of considering viability assessment but has been adopted on other multi phased schemes where it would be inappropriate to use a direct residual value comparison with the base land value.

The IRR is the rate of return that would make the present value of future cash flows plus the final market value of an investment or business opportunity equal the current market price of the investment or opportunity. The internal rate of return is an important calculation used frequently to determine if a given investment is worthwhile. An investment is generally considered worthwhile if the internal rate of return is greater than the return of an average similar investment opportunity, or if it is greater than the cost of capital of the opportunity.

Information required in a development viability assessment:

In making a case that viability is an issue in meeting planning policy obligations, it is implicit that the viability assessment includes sufficient information to enable the local planning authority to evaluate the report. The report should include an explanatory

assessment with detailed supporting information. This information should comprise the following details (in both hard copy and electronic form):

- a) Planning application details - plans, design & access statement, sections, elevations etc. as relevant
- b) Supporting reports for site abnormalities, schedules of condition etc
- c) QS cost assessment- The evidence should include a current day full build cost estimate, not summary, showing how the costs have been estimated (and include a full breakdown of both gross and net internal areas).
- d) Market evidence- This needs to comprise:
 - (i) Estimate of sales/rental values of each individual unit of accommodation;
 - (ii) Sales Market reports together with evidence in support of the sales/rental values adopted;
 - (iii) Sales rates assumptions;
 - (iv) Values assessed for affordable housing (if applicable).
- e) Detailed valuation reports for the current market value of the site (include tenures, easements, description etc). This needs to include a valuation of the site in its existing or potential or alternative use with an explanation showing how these values have been assessed and supporting evidence as appropriate.
- f) Viability appraisal including cash flow. This needs to be provided in an electronic file format to enable us to review the calculations.

5. ASSESSMENT PROVIDED BY THE APPLICANT

The report provided by Savills is fairly comprehensive and has been evidenced by the following documents as appendices to their report:

- Appendix 1 – Site Location Plan
- Appendix 2 – Scheme Masterplan and Block Drawings
- Appendix 3 – Development Specification
- Appendix 4 – Proposed Accommodation Schedule
- Appendix 5 – Existing Accommodation Schedule
- Appendix 6 – G&T Existing Use Refurbishment Costs
- Appendix 7 – Existing Private Values Summary
- Appendix 8 – Existing Affordable Appraisal
- Appendix 9 – Existing Retail Values Summary
- Appendix 10 – Existing Office Values Summary
- Appendix 11 – EUV Appraisal
- Appendix 12 – Savills Proposed Residential Values Report
- Appendix 13 – Proposed Affordable Appraisal
- Appendix 14 – CBRE Proposed Retail Values Report
- Appendix 15 – Farebrother Proposed B1 Office Values Report
- Appendix 16 – G&T Proposed Build Cost Estimate
- Appendix 17 – G&T Budget Savings Letter
- Appendix 18 – Escalation Rates
- Appendix 19 – LL Cost Trend & Forecast Report
- Appendix 20 – Oxford Economics House Price Report
- Appendix 21 – Draft Heads of Terms
- Appendix 22 – E&C Financial Appraisal Model

Gross development value (GDV):

a) Market sales values

It is DVS opinion that Savills pricing proposals is broadly reasonable, particularly given the lack of strong evidence. DVS consider that the low and mid rise average values are broadly correct but question whether the tower buildings averages are pessimistic. DVS consider that the evidence from the Strata tower is slightly misleading due to the specification, maintenance and marketing history.

Whilst the provision of a large number of towers in close proximity does call into question whether the premium that this type of accommodation provides will lose its exclusivity (and therefore value) and the impact of restricted views. Nonetheless there will be some stunning views from many apartments, for instance overlooking the Shard at London Bridge as well as more established views of Canary Wharf, the City and the West End. We would not be surprised if significantly better values are not achieved in this element of the scheme.

Therefore, we have considered what the impact of an overall increase of 5% would have on the development viability.

b) Affordable housing values.

There are a number of issues to consider when looking at the affordable housing values. Consideration needs to be given to both Southwark's policy and how this sits within the context of the London Plan.

The London Plan seeks to maximise affordable housing without a specific target, however, Southwark policy is explicit and requires 35%. In addition to meet the need of the specific circumstances pertaining in Southwark there are other policies that need to be considered for example there are issues regarding affordability and Southwark's policy is more explicit than the London Plan and set lower salary thresholds which have an impact on the value of shared ownership tenure. Southwark are also currently still promoting the use of target rent rather than affordable rent.

I understand that the Annual household income range mid-point for intermediate housing units in Southwark for 1, 2 and 3 bed incomes are (range mid-point) £29,515, £35,943 and £42,372 respectively.

Whereas the Mayors guidance is that Local planning authorities should seek to ensure that intermediate provision provides for households with a range of incomes below the upper limit, and provides a range of dwelling types in terms of a mix of unit sizes (measured by number of bedrooms), and that average housing costs, including service charges, to households for whom intermediate housing is provided are affordable by households on annual incomes of £42,150 pa (i.e. the midpoint of the range between £20,000 (updated from AMR 7 in line with RPI) and £64,300). On this basis, average housing costs, including service charges, would be about £985 a month or £230 a week (housing costs at 40% of net income, net income being assumed to be 70% of gross income).

I have reviewed the affordable housing figures included in both the EUV calculation and the Financial Model and these do not appear to be consistent.

In relation to the EUV a target rent calculation has been undertaken which appears to make reasonable assumption, however, in the EUV appraisal Savills have adopted the rent cap levels.

"7.2.14 We consider it a reasonable assumption that an Registered Provider would seek to apply full rent caps for each unit type."

I assume on this basis that the refurbished estate would justify a higher figure however, they do not appear to have done this for the proposed development as a similar statement is not included in Section 9 of the report and they have arrived at there figures having regard to their experience in dealing with RSLs.

I understand to a certain degree why there is a difference in the rates per square foot but in my opinion this can not be justified on size difference between proposed and refurbished as the average sizes are only approximately 10% larger in the proposed scheme or that the existing scheme also has significantly higher number of the smaller flats although I do recognise that this would skew the average figures to some extent.

I have attempted to analyse the figures and it is my view that if the calculations were consistent a similar price per square foot would be adopted for both scenarios. It should be noted no specific evidence has been provided to support the figures and in view of the issues highlighted on the two approaches further information should be provided prior to any discussion regarding different tenure mixes being adopted.

Savills have adopted a rate of £99 per sq ft for the proposed development and this seems a conservative estimate, however, the figure adopted in the EUV is an average rate of £142 per sq ft which seems excessive.

I have undertaken my own analysis on both schemes and in respect of the proposed development the capped rents will definitely be triggered in respect of the 3 bed units and possibly on the 2 bed units although not on the 1 bed, this result's in an overall rate of approximately £127 per sq ft before any on-cost deduction if appropriate. Savills analysis shows the 1 and 2 bed units below the rent cap. In arriving at this analysis I have adopted similar deductions to those used by Savills on the EUV calculation as they do not appear to have explicitly stated what the deductions are used for the proposed development.

In relation to the existing stock the overall rate on the calculated target rents assuming no further uplift would be circa £105 per sq ft. Savills have argued that any RSL would have the right to charge the capped rate, however, I would argue that this is a refurbishment of an existing estate and the rents reflect the improvements and quality for the space already so to increase the rents beyond this to a level that would be adopted on a brand new scheme seems an optimistic assumption.

In relation to the Shared Ownership accommodation Savills have adopted £225 per sq ft as the base rate and having regard to Southwark's affordability criteria this appears to be a reasonable assumption. In order to achieve this threshold the rent on the remaining equity is reduced below the standard 2.75%. Savills have used variable rates in these calculations between [REDACTED] in addition they have adopted a [REDACTED] reduction on the market value which I assume reflects a different standard of finish compared to the market units. I would normally expect the shared ownership properties to be valued at the same rate and be finished to similar standard as the private housing. The implications however are minimal as higher values would probably result in lower residual rents to maintain affordability.

No grant has been assumed and this is in line with current guidelines.

c) Commercial properties

Retail

CBRE were instructed by Lend Lease to report on Retail and Leisure elements and their report is dated 26 April 2012.

CBRE emphasise the uniqueness of the scheme stating there are no similar comparables.

The scheme will provide circa 100,000 and 120,000 sq ft of net space which CBRE considers sufficient to create critical mass yet if it were larger it would need to incorporate traditional department stores and larger floorplates.

They consider the impact of the E&C Shopping Centre that is planned to be redeveloped by St. Modwen but consider that the Heygate retail proposals will complement rather than be negatively impacted.

There are three distinct zones for the retail:

Walworth Road – 27,325 sq ft GIA proposed

This is proposed to compromise a typical High Street mix with a focus on multiples. Existing demand for units is strong, driven by local community shopping. However, in this part of the development it is noted that if St. Modwen's Shopping Centre is redeveloped it may well compete for tenants.

New Kent Road

This location may have double height units and will aim to cater for specialist retailers, probably reflecting that this is more of a destination pitch due to lack of a draw to the northern side of the road which comprises residential and secondary office space.

Central Shopping Street

This is retail fare designed to attract independent retailers. CBRE seem to indicate the challenge in making this part of the scheme work. Many of new shopping areas that have developed in London over the last decade benefit from a large number of office users which help keep them vibrant during the day. Box Park, a recent development located in converted shipping containers has started from scratch, similarly to E&C, it is located close to an underground station but it has a high number of office users nearby and provides small units in an improving location.

CBRE recommend to make this space successful requires:

A street market

Locating a Foodstore to encourage footfall through the development

Allow flexible lease terms

Creating a "sense of place"

Ensuring strong A3 to encourage people to spend time in the development

CBRE have given guidance suggesting that A3 uses could be increased at the expense of A1 and some units might be increased in size.

The applicant's supported by CBRE are proposing rents at the following levels:

Supermarket - [redacted] per sq ft

Showroom rents of [redacted] per sq ft

Retail rents vary between £ [REDACTED] per sq ft in [REDACTED] and £ [REDACTED] per sq ft in [REDACTED]

Local evidence has been provided, existing units are not really comparable due to that regeneration has yet to happen. Rents along Walworth road are difficult to quantify as they are assessed on a Zone A rather than an overall basis. The retail at Strata has not let with quoting rents now at £15 per sq ft.

CBRE have provided evidence of lettings at Box Park, More London, Bankside and Goodmans Fields which given their advantageous river or City fringe locations broadly support the adopted values.

Sainsbury's have according to CBRE taken a pre let of 15,000 sq ft fronting New Kent Road at £20 per sq ft.

The applicant has not evidenced yields but have adopted level of [REDACTED] for all the retail, leisure and supermarket units.

Broadly, particularly given the challenges facing retailers currently - whether independents or large multiples, DVS do not have an issue with this level. However, we do consider that given the relatively modest rental level we would not be surprised if a keener yield was achieved on the supermarket, which tend to have very strong covenants.

Retail Conclusion

DVS broadly agrees with recommendations made by CBRE in their report. We have considered both evidence provided and recent lettings and consider that the applicants proposals are reasonable. Having seen reports on supermarkets, which due to long leases and strong covenants are bucking the retail down turn, and based on other developments, consider that the supermarket may be undervalued in the order of £1.2 to £2m capital value.

Offices

The scheme proposes 51,000 sq ft of net office space. The specification has not been confirmed so Farebrother Chartered Surveyors, who have undertaken a report for the applicant, have assumed the units would be finished to a Category A finish, which we take to mean fitted out space with some form of air cooling. The alternative would be for

the developer to leave the space as a shell finish and pay incentives to compensate the tenant for fitting out.

Farebrother, correctly in our view, state that the current rental stock in and around Elephant and Castle is not reflective of what is proposed and have looked further afield; south of the river up to the prime markets of Bankside with the likes of the Blue Fin Building and More London to more fringe locations that have been subject to regeneration such as Bermondsey.

Having assessed these different locations they have proposed adopting a range of rents from [REDACTED] per sq ft.

DVS is broadly comfortable with these figures and they tie in with the figures negotiated on Eileen House scheme between DVS and Shaw Corporation at £28 per sq ft, albeit a couple of years ago.

They expect most leases to be let on five year terms and a nine month rent free period. They have also assumed an average of nine months void from practical completion. A yield of [REDACTED] has been proposed. DVS consider that all these assessments fall within a range considered appropriate to adopt.

d) Others- such as car spaces, ground rents etc.

The assumptions used seem to be generally reasonable and any amendments would have limited effect on the overall scheme viability of the scheme.

Gross Development Costs (GDC):

a) Build costs.

- I. The assessment assumed that what was provided for in the G&T cost plan is the overall scope of works required. If confirmation is received that allowances were made for Phase 1 works and anything outside the boundary should not be considered, obviously these should effectively be taken out from both assessments.
- II. Where items can not be validated due to the absence of further evidence by way of reports, back up calculations, etc. these figures remain in the DVS assessment.

- III. The original submission amounts to circa £████████. Adjusting this to reflect current cost at 3Q2012 utilising BCIS Tender Price Indices for the purposes of this exercise would equate to circa £████████.
- IV. The current DVS order of cost estimate is circa £████████, £████████ (5%) less than G&T's adjusted figures at 3Q2012. This level of difference is not considered unreasonable at this stage and design of development.
- V. A letter was provided by G&T as part of Savills Viability Assessment (Appendix 17) which suggests that potential savings can be achieved by 2% to 3%.
- VI. If a saving is applied utilising 2.5% (average), then the DVS order of cost assessment is circa £████████ (2%) less than G&T's adjusted figures at 3Q2012. The difference still being not unreasonable at this stage and design of development.
- VII. Benchmarking exercise was provided by G&T to validate the overall cost per m² rate provided for this scheme. It is assumed that the benchmarking is adjusted to cost and time factors.
- VIII. It is assumed that the rates adopted would cover the likely specification for this scheme commensurate with the sales / values.

b) Abnormals.

All aspects of the development costs have been consider by the QS and this is covered in above and at appendix 2.

c) Contingency.

The scheme contingencies are generally ██████ on all aspects of construction, however, it was noted that ██████ was used in respect of utilities reinforcement; however, this will have minimal impact.

d) Professional fees.

The figure adopted is purported to be around ██████ but if you analyse the summary the figure equates to around 1████% and this is explained by a separate project

management fee of [REDACTED] % on the construction, infrastructure and design costs. This seems excessive as I would expect to see a maximum of 12.5% with this including the project management fees.

There is also a Development Management Fee of [REDACTED] %, this could potentially be described as additional profit, therefore, if this figure is to be retained the profit target should be reduced to reflect this or preferably this fee should be removed entirely from the Financial Model.

e) S106 & CIL obligations.

No CIL estimated is included in the model, which I do not understand as the rate has been published and the areas are known. I appreciate there maybe an issue as to whether it is calculated on an uplift approach or on the whole, but a figure could have been included even on a worst case scenario basis.

I have undertaken a calculation and would estimate that the CIL payment is likely to be between £6-9.1 million.

The section 106 contribution is £2,913,160 and a payment for Transport for London of £11,683,495.

Ideally I would like clarification of the policy compliant requirements of the scheme and confirmation that the figure adopted are in line with this.

f) Marketing costs

These will generally be sales agency, marketing (Show home, advertising etc), and legals.

The financial model includes selling costs at [REDACTED] % and it is assumed this includes, marketing, agents fees and legals, overall this is probably not unreasonable for a scheme of this nature.

In addition to sales costs on the private there are also sale costs on the affordable and this has been taken at [REDACTED] %, this seems a little higher than I would have expected but overall would have minimal effect on viability.

g) Finance

Finance interest and finance costs are primarily affected by the amount of money borrowed and repaid throughout the development period from commencement of the scheme (ie the preliminary period) to the final sale. The actual applicant's arrangements are not what should be considered, but those for a typical developer of the application scheme. The HCA DAT User Guide explains this well:

"3.12 Finance cost 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. It depends 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. If the developer has other variable borrowings (such as an overdraft), or other investment opportunities, then the value of credit balances in reducing overall finance charges is potentially the same as the debit interest charge. If not, and the developer would simply put the funds into the bank, then a lower rate is appropriate."

Finance has been based on 100% gearing at a rate of **[REDACTED]%**, this seems to be a bit higher than other schemes I have reviewed over the last year or so, I would have expected to see 7% which would include arrangement fees.

The **[REDACTED]**% has been derived from a **[REDACTED]**% 10 year swap rate plus a **[REDACTED]**% margin and **[REDACTED]**% for fees. I would like to see some justification for the swap rate as these have reduced significantly since 2011.

I have undertaken some research into current swap rates and it seems that there has been a reduction over the last 12 months with rates for small loans falling back from around 4% to nearer to 2%, however, the ability to obtain funding is extremely difficult at the moment and large liabilities that front load this project will potentially effect the funding capability.

In order to review the impact of finance in the Financial Model I have included a scenario at 7% as well as at the adopted rate of **[REDACTED]**%

h) Disposal programme.

The approach taken in the Financial Model assumes [REDACTED] % pre-sales prior to construction commencing on a particular phase, once construction has commenced marketing will resume on that phase after month [REDACTED] and it is assumed that a further [REDACTED] % will be sold prior to practical completion. The remainder of the units are then sold in the next [REDACTED] quarters.

Essentially there will be various overlapping period as the different phases and blocks within those phases are commenced. The average completions across the development are around [REDACTED] units per year and this in my opinion is a fairly aggressive policy in view of competing developments in the locality.

i) Growth and Inflation

The applicant has provided a financial model which allows for escalation of both costs and values, having regard to supporting documents produced by other consultants.

The escalation adopted depends on the input and therefore reflects the different inflation that each element might attract. The escalation figures in relation to the values are made up of two parts, a general inflation figure and a regeneration effect.

It is interesting to note that whilst the property market generally works in cycles the growth pattern for the financial model is upwards only and in view of the timescale this is probably optimistic, however, you also need to consider the delivery period and whilst the escalation is shown through to 2035 the majority of the development is delivered by 2028.

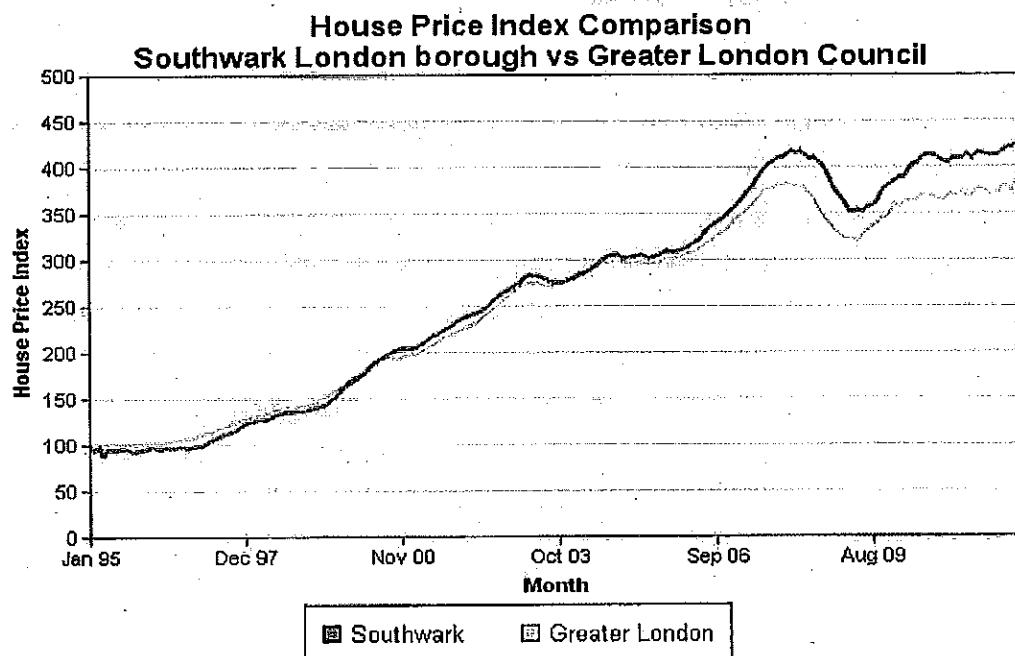
The regeneration effect also continues for a longer period than I would have expected, as there will come a point when the scheme either has succeeded or is struggling to get established. It is my view that once the development has become established there will be a honeymoon period after which the rise in the values is likely to tail off, particularly as there will be second-hand market beginning to be established by the end of the development period.

In relation to the forecasting whilst this is impossible to predict with any certainty, the base inflation figures suggested by Savills reflect an increase over the 15 year life span of the scheme that appears on the conservative side of reasonable when

compared with the average over the last 17 years or even over the last 35 years. However, past performance is not a guarantee of future performance and the economic circumstances that existed across the previous property cycles are very different to those that exist today.

The major issue is affordability and the availability of money; this has changed a lot over the past 10 years as salary inflation has been relatively modest compared to house price inflation. There are also other considerations as London is attractive to foreign investors, the health of global economy will have an impact and the ongoing issues within the Eurozone may see further investment in London as it is regarded as a relatively safe economy.

I have looked at the land registry data for average house price rises over the last 17 years in LB Southwark and this shows an average rate of 8.74% pa,



The Nationwide publishes indices for Greater London tends to support these figures. I have also looked at the Nationwide Index running from 1973 through to 1995 and this gives an average increase over this period of approximately 8.22% and an average of 8.55% over the 37 year period.

The averages mask major variations; the Nationwide Regional Quarterly Indices for Greater London show the following.

Period		Average per annum increase	Comment
Q4 1973	Q2 2012	8.55%	Overall
Q4 1973	Q4 1989	14.15%	To 1980's peak
Q4 1989	Q4 1992	-8.81%	Peak to Low
Q4 1989	Q4 2007	6.76%	Peak to Peak
Q4 1992	Q4 2007	10.65%	Low To Peak
Q2 1992	Q2 2012	7.36%	Low to Current Day
Q2 2007	Q2 2012	0.67%	Since Credit Crunch

The Land Registry Figures for Southwark

Period		Average per annum increase	Comment
Jan 1995	May 2012	8.74%	Overall
Jan 1995	Feb 2008	11.53%	Low to peak
May 2007	May 2012	2.51%	Since Credit Crunch
Feb 2008	Jun 2009	-13.78%	Peak to Low
Jun 2009	May 2012	6.95%	Low to Current

I appreciate that over a development of this length there is potential for spikes in the general trend there is also the possibility that the market could see another complete cycle before the scheme is fully developed and sold. The best fit line over the last 17 years shows the assumptions made by Savills are slightly below this line.

The growth figures adopted by Savills also included a regeneration premium of **[REDACTED]%** which runs from 2018 to 2035, however, the delivery of the housing according to the financial model is between 2018 and 2028.

The average annum increase reflects **[REDACTED]%** from 2012 through to 2028 on the base inflation figures and **[REDACTED]%** on the "regen" inflated figures.

	Base Inflation	Regen Inflation
2007	1.0%	1.0%
2008	1.0%	1.0%
2009	1.0%	1.0%
2010	1.0%	1.0%
2011	1.0%	1.0%
2012	1.0%	1.0%
2013	1.0%	1.0%
2014	1.0%	1.0%
2015	1.0%	1.0%
2016	1.0%	1.0%
2017	1.0%	1.0%
2018	1.0%	1.0%
2019	1.0%	1.0%
2020	1.0%	1.0%
2021	1.0%	1.0%
2022	1.0%	1.0%
2023	1.0%	1.0%
2024	1.0%	1.0%
2025	1.0%	1.0%
2026	1.0%	1.0%
2027	1.0%	1.0%
2028	1.0%	1.0%
2029	1.0%	1.0%
2030	1.0%	1.0%
2031	1.0%	1.0%
2032	1.0%	1.0%
2033	1.0%	1.0%
2034	1.0%	1.0%
2035	1.0%	1.0%

Overall I think it is reasonable to take this approach in order to maximise the affordable housing they can deliver, however, the escalation continues well beyond the proposed delivery period, therefore, the difference between the base inflated prices and the values with the regeneration effect added are not as significant as first envisaged.

The analysis shows that Savills regeneration inflation has the following effect at various delivery stages.

	Timing of Delivery		Regeneration Effect Uplift on Value for the relevant period
		Cumulative	
2018-2020	[REDACTED]	[REDACTED]	[REDACTED]
2021-2022	[REDACTED]	[REDACTED]	[REDACTED]
2023-2025	[REDACTED]	[REDACTED]	[REDACTED]
2026-2028	[REDACTED]	[REDACTED]	[REDACTED]

It is my view that the regeneration effect will be more marked for a period once the development has established and will become less as the development nears its completion.

I have run the following scenario to see what difference there would be if the effect is less uniform.

	Base Inflation	DVS Regen Inflation
2012	%	2.40%
2013	%	0.80%
2014	%	2.60%
2015	%	4.60%
2016	%	5.90%
2017	%	6.00%
2018	%	7.90%
2019	%	9.00%
2020	%	10.40%
2021	%	8.50%
2022	%	8.50%
2023	%	7.50%
2024	%	7.50%
2025	%	6.50%
2026	%	6.50%
2027	%	5.50%
2028	%	5.50%

When input into the financial model with no other changes it reduces the perceived profit gap at [REDACTED] % on costs by £40 million and increases the IRR from [REDACTED] % to [REDACTED] % and the profit on cost increases more noticeably. The analysis of this change is as follows:

	Timing of Delivery		Regeneration Effect Uplift on Value for the relevant period
		Cumulative	
2018-2020	[REDACTED] %	[REDACTED] %	[REDACTED] % - [REDACTED] %
2021-2022	[REDACTED] %	[REDACTED] %	[REDACTED] % - [REDACTED] %
2023-2025	[REDACTED] %	[REDACTED] %	[REDACTED] % - [REDACTED] %
2026-2028	[REDACTED] %	[REDACTED] %	[REDACTED] % - [REDACTED] %

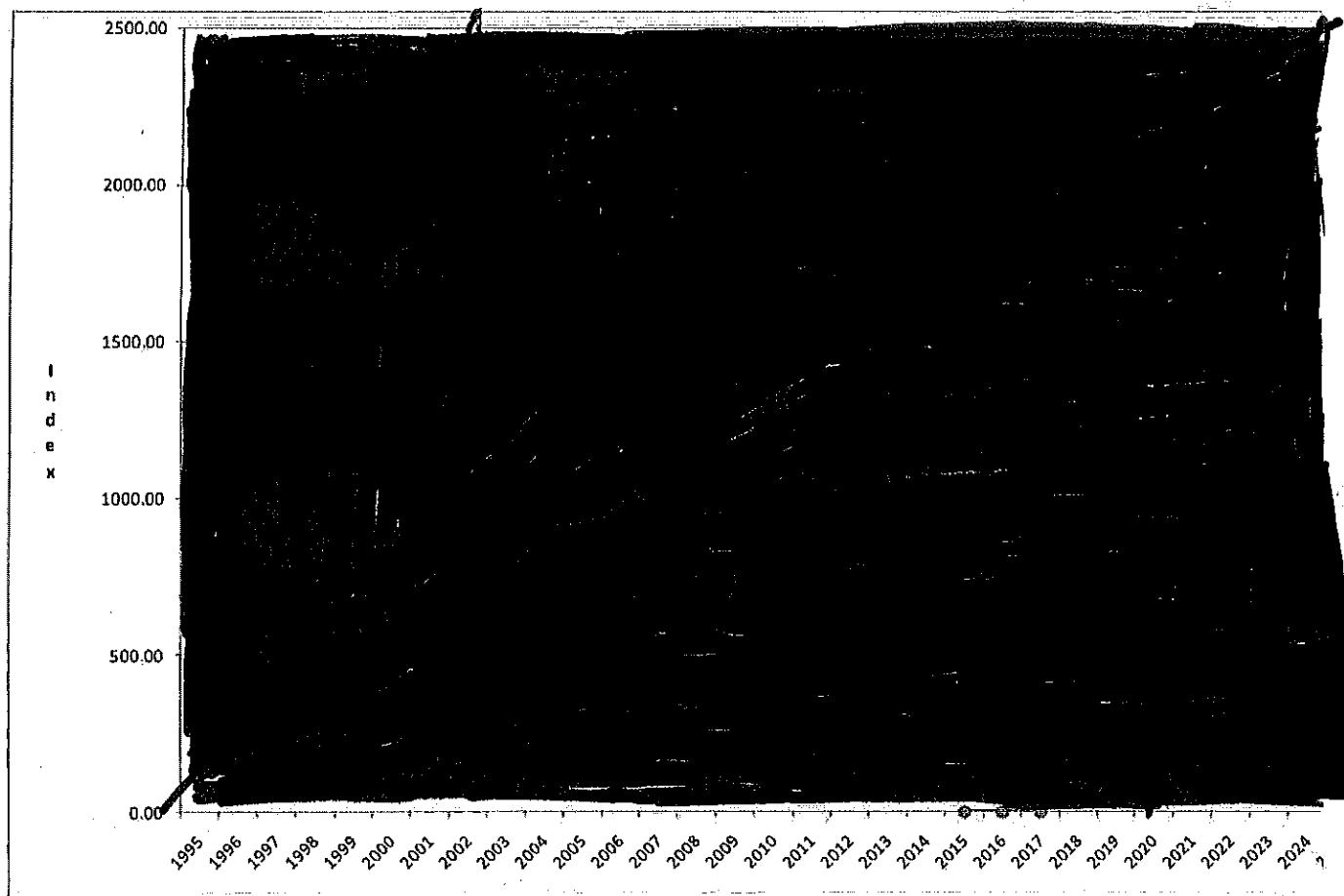
The impact of these two scenarios is demonstrated in the graph over leaf and is overlaid with residential area delivered relating to the time period.

Escalation is also applied to the build costs with a long term average of [REDACTED] % and the affordable housing has been escalated at [REDACTED] % above CPI which has been taken as the long term forecast of [REDACTED].

I do not have any particular issue with the forecast in relation to the costs.

RESTRICTED

Land Registry Index for Southwark with Savills Growth Assumptions for 2012 and beyond.



RESTRICTED

j) Profit.

Savills have adopted a [REDACTED] % on cost approach and identified a significant gap between that and what the escalated model currently shows, they are looking to close this gap by various approaches including the enhancement of the affordable housing value through tenure changes.

I do not accept the profit benchmark that Savills have adopted, I think it is unrealistic to look at profit on cost basis for a development of this type, an IRR approach would be more appropriate. The approach is extremely crude and as can be seen from the scenarios table similar IRR's can produce different levels of profit on cost.

Within the Financial Model they have also adopted a Development Management Fee of [REDACTED] %, essentially this is profit, if this to be retained the profit target needs to be reduced or this needs to be removed from the Model.

I would like to clarify what [REDACTED] % on cost represents as an IRR as the current [REDACTED] % on cost reflects an IRR of [REDACTED] %. In respect of target rates for IRR I would anticipate a figure of between 15-20% but in reality whether this would be achieved for a scheme of this nature is debateable. It is interesting to note that in the Savills report Table 13 shows a range for the IRR of [REDACTED] % for scheme with planning permission and as we are assuming that planning is granted within this exercise it seems more appropriate for the profit to lie in this range rather than [REDACTED] % to which they refer.

I would like to see some evidence provided to benchmark these levels of returns as my understanding is that most development schemes when analysed following completion average out below 15%.

The IRR benchmark quoted in the Savills report is [REDACTED] % and this compares with often quoted levels of 15-20% on development schemes, however, the perceived profit gap is calculated by way of the crude methodology on profit on costs.

Therefore prior to major decisions being taken to reduce the perceived profit gap, the gap actually needs to be identified and this in my view is significant less than £[REDACTED] m identified. I have undertaken some simple analysis on the profit benchmark and for each reduction in the profit on cost of 2.5% results in the gap reducing by £[REDACTED] m. However, at the lower end of my analysis there is still a gap of £61.6.m based on Savills inputs. This analysis is extremely crude and I believe there should be more reference to the IRR but this requires running a number of scenarios to see what could result in an acceptable return.

Residual land value (RLV).

NPPF requires the applicant to demonstrate that a planning policy compliant scheme is unviable. This means the assessment should show viability results assuming a policy compliant scheme. If this is correctly done, the deduction of GDC from GDV produces a net residual site value (RLV) which is compared to the Benchmark value. If the RLV is in excess of the Benchmark, the scheme is viable.

The residual land value for a policy compliant scheme on a current cost/current value basis is negative and as result is clearly unviable. This is ascertained by using an un-escalated version of the model and increasing the affordable housing requirement to 35%, the results show deficit of over £500 million much of which is finance costs.

Adopting the Savills assumptions the escalated version of the model at 35% produces a deficit of approximately £30 million where on their figures they would be looking to make a profit of £ million.

Benchmark value:

Savills have adopted a benchmark land value of £48 million which is the agreed purchase price with Southwark this has been justified by undertaking a valuation on an existing use basis, as well considering a market value approach.

Savills decided not put forward an alternative use value at this stage but did reserve the right within their report to consider this at a later date.

The existing use approach was based on a refurbishment of the current estate plus an uplift of 30% as a landowner premium. Savills have provided a development appraisal to demonstrate the value and provided 6 separate appendices with supporting information which cover;

Existing Accommodation Schedule

G&T Existing Use Refurbishment Costs

Existing Private Values Summary

Existing Affordable Appraisal

Existing Retail Values Summary

Existing Office Values Summary

EUV Appraisal

Details of the existing residential unit mix has been provided and relied up on for assessing the benchmark figure and this includes the tenure mix.

The residual value shown in the appraisal is £37.3 million once the premium is added the figure adopted is £48.5 million. I do not accept that there is a need to provide uplift in this situation; the policy compliant value of the site is well below the existing use value and therefore, the residual value fairly reflects the value of the property. Savills do not justify the arbitrary figure of 30% other than it results in the increase in the residual value above the figure agreed with Southwark Property.

The site at present is likely to be producing limited income; however, there are potential ongoing liabilities and unless there is a capability to take on a refurbishment this will continue. Therefore I am not convinced the landowner in these particularly circumstances would require an uplift of this nature.

I have reviewed the market evidence used to establish the Gross Development Value adopted in the EUV valuation and I am of the opinion that figures adopted appear reasonable for the refurbished local authority stock.

In relation to the affordable housing the calculation of the target rent appears to be reasonable, however, the figure adopted in the appraisal is based on a valuation adopting the national capped rate. I do not accept these figures as the calculated target rents are well below the national caps and I am not convinced that it is justified to show such a large uplift as this is only a refurbishment of the existing estate. The overall rate per sq ft adopted actually works out in the Savills appraisals at more than 40% higher than they adopted in the proposed scheme although some of this is explained by unit size and mix.

The allowance within the G&T cost plan in refurbishing the existing buildings assumed that minimum works will be carried out in order to keep the buildings habitable and usable. It is assumed that the scope of works provided by G&T is correct and that the values / sales should reflect what is expected for that minimum works provided. See appendix 2 for the cost analysis.

In order to justify the purchase price Savills have also considered the market value having regard to the sales of develop sites.

Savills have provided limited details of market evidence but these are difficult to analyse as they provided no details of whether planning permission already exists, whether the site are subject to a planning brief or master plan. The circumstances of each site also need to be taken into account as there will be different individual factors affecting the site and adjustments need to be made to the sale price which would render the evidence to be of limited use.

However, Savills interpretation of the evidence is such that they have adopted the lower end of the price per acre and have calculated a figure of £72 million.

In light of the EUV and MV, Savills conclude that the purchase price of £48 million agreed with LB Southwark is considered to be reasonable and have adopted this figure as fixed land value within the Financial Model.

When considering the Benchmark value I have had regard to the emerging RICS guidance in relation to the benchmark figure.

Site Value either as an input into a scheme specific appraisal or as a benchmark is defined in the guidance note as follows:-

"Site Value should equate to the market value subject to the following assumption: that the value has regard to development plan policies and all other material planning considerations and disregards that which is contrary to the development plan."

The assessment of market value with assumption is not straightforward but must, by definition, be at a level which makes a landowner willing to sell, as recognised by the NPPF. Appropriate comparable evidence, even where this is limited, is important in establishing Site Value for scheme specific as well as area wide assessments.

The use of the term Existing Use Value is in itself somewhat confusing as this is defined in the RICS Red Book as an approach for accountancy purposes. EUV is also often referred to as Current Use Value which is essentially the market value reflecting only the current use of the property. Current Use Value does not reflect the workings of the market as land does not sell for its CUV, but rather at a price reflecting its potential for development. While the use of CUV plus a margin does, in effect, recognise hope value by applying a percentage increase over CUV, it is a very unsatisfactory methodology when compared to the market value approach set out in the RICS guidance.

I have reviewed the appraisal undertaken by Savills in respect of the refurbishment approach and consider that £37.3 million potentially overstates the position irrespective of whether an uplift is warranted. In the current market a refurbishment project of this nature is a massive undertaking particularly as the estate is essentially vacant.

The main area of disagreement is the Gross Development Value where I consider the social rented tenure is valued too high, however, the difference is reduced as DVS consider the refurbishment costs would be lower and the developers profit would be lower in view of the fact this is largely an affordable housing development with over 90% of the units for social rent.

I have undertaken my own appraisal for the refurbishment scheme and have adopted a figure of £26.4 million.

6. DVS ASSESSMENT OF VIABILITY.

I have not in this case undertaken my own appraisals but have worked with the Financial Model provided to run various scenarios to test the profitability of the scheme.

I have run the Model initially with escalation and 35% affordable housing (Scenario 27) to establish whether a policy compliant provision can be made, it is clear that this produces a deficit or insufficient profit to commence a project of this nature.

The scenarios I have run are as follows

INPUTS	
Residential	Base figure or 5% uplift
Costs	Either adopted -2.5% or DVS -3.25%
Finance	7% or 7.5%
Land Value	£48 million or £26.4 million
PF – Professional Fees	[REDACTED]
PM – Project Management Fee	[REDACTED] % has been reduced to 1%
DM – Development Management Fee	[REDACTED] % removed from calculation
CIL	£9.04 m
Escalation	Savills base +2% or DVS profile as stated above
Affordable %	General 25% but 3 scenarios at 35%
Intermediate Value	As adopted by Savills
Social Value	General Savills adopted figure

The results are shown in the table below, the result row for the IRR has been formatted with red meaning it will not achieve an acceptable return, the amber is showing a return that is marginal and the green should be an acceptable return.

It can be seen that while the IRR is providing consistent figures the profit on cost varies more noticeably and this is to some degree down to the fact the IRR analysis ignores the cost of funding.

Scenario Analysis

7. INITIAL CONCLUSIONS.

I have carried out a detailed review of the applicant's viability appraisal and concluded that:

- a) The information provided was extensive and detailed, however clarification was required with respect to a number of inputs and this was provided following meetings and telephone discussions however further clarification is still required on certain points.
- b) The viability methodology used is broadly acceptable.
- c) The inputs used in the Financial Model are generally acceptable with most of the inputs being within an acceptable tolerance however, the cumulative effect of making minor changes to the figures can be fairly significant as shown in the scenario analysis.
- d) The Financial Model demonstrates that the applicants figures are very sensitive to change, it is my view that a profit level of between 15-18% would be acceptable but consideration needs to be given to the profitability of the early stages of the development otherwise deliverability becomes an issue so I have set a benchmark level of 16% IRR [REDACTED]
[REDACTED]
- e) It would be useful to have some benchmark analysis similar to that which the IPD produce for property investment and commercial development to put the results into context.
- f) I consider that the benchmark site value to be slightly high although the overall impact of the difference in isolation is minimal, however, in the round it does have relevance and the agreed purchase price does have implications on the viability.
- g) Due to the nature of the development there would be an opportunity to engineer cost savings in relation to the development costs over a scheme of this length. It is my view that initially the developer is more likely to see an improved return from savings made in the procurement and design of the development than growth in capital values as this is in their control, this to some extent has been recognised in the G&T side letter at Appendix 17.

- h) The scenario results demonstrate that a 5% improvement in the sales values has significant impact on the profitability and this only underlines the need to have a review mechanism to ensure the gap between any concession on affordable housing or section 106 and policy compliant requirement is recouped if the scheme is more successful than currently anticipated. However, in drawing up any such mechanism it is important, not to make the mechanism so restrictive it acts as a disincentive.
- i) Prior to discussing whether there is a need to vary the tenure type to enhance the affordable housing, it is important to identify what an acceptable target profit rate is, so that further scenarios can be run. The scheme currently does not appear to be able to support a policy compliant provision but an acceptable return needs to be identified so that further scenarios can be measured.
- j) It is my view that profit short fall could be as low as £30 million in which case some changes to the tenure may enable this to be reduced, however, if the profit gap is any greater it is unlikely that a change to the tenure types alone would reduce the gap sufficiently.

8. POST INITIAL CONCLUSION DISCUSSIONS AND OUTCOMES

Following on from the initial draft report there were a series of meeting to discuss the various differences in order to reach more of a consensus, however, due to the size of the scheme there are always going to be differences but the aim was to provide advice which will lead to the regeneration being delivered.

In relation to the financial model various elements were identified and the outcomes are as follows;

- Private Revenues: It was agreed to use the Savills revenue figures;
- Affordable Revenues: It was agreed to assume rent caps on both the EUV and Proposed schemes the updated appraisal reflecting the proposed scheme at rent caps resulted in a net increase of approximately £1.41m;
- CIL: The appraisal now includes a CIL payment of £9.1m, for the purpose of the viability model;
 - Finance Rate: The interest rate of 7.5% adopted is derived as follows:
 - Base Rate (10yr Swap) – 2.0%
 - Margin – 4.0%
 - Fees – 1.5%
 - TOTAL = 7.5%
- In support of this assumption, Lend Lease provided indicative terms from ██████████ in relation to the St. Mary's Development. For the purpose of this scheme DVS is willing to accept the proposed finance rate due to the nature and length of the scheme and the initial costs.
- Benchmark Land Value: It was agreed that the Purchase Price of £48m would be adopted as the fixed land value and that the GLA had not raised any issue with regard to this at this stage. This has an impact on the IRR of approximately 1.3% compared to adopting the lower value originally highlighted in the DVS draft report.
- Cost Plan: The DVS QS had a number of discussions with G&T over the development costs and has now broadly accepted the figures with a 2.5% discount in line with those figures adopted in the financial appraisal.

- Professional Fees: a detailed breakdown was provided. The total fee is in the range of [REDACTED] % to [REDACTED] % (inclusive of the PM fee). The midpoint is [REDACTED] % which has been used in Lend Lease's model although this excludes the separate development management fee. In the fee analysis the Project management fee is shown at [REDACTED] % with the statement "as per development agreement" I am unclear as to what this means and why should this figure be stipulated in the development agreement and for what purpose. Essentially the aspect of the fees has not been resolved therefore the scenarios for the Financial Model reflect these differences.

Savills have run figures on the affordable rent option and shared ownership affordability criteria which they have provide to me, this results in an increase in the affordable housing value by approximately £[REDACTED] million on a day one basis which is approximately [REDACTED] % uplift.

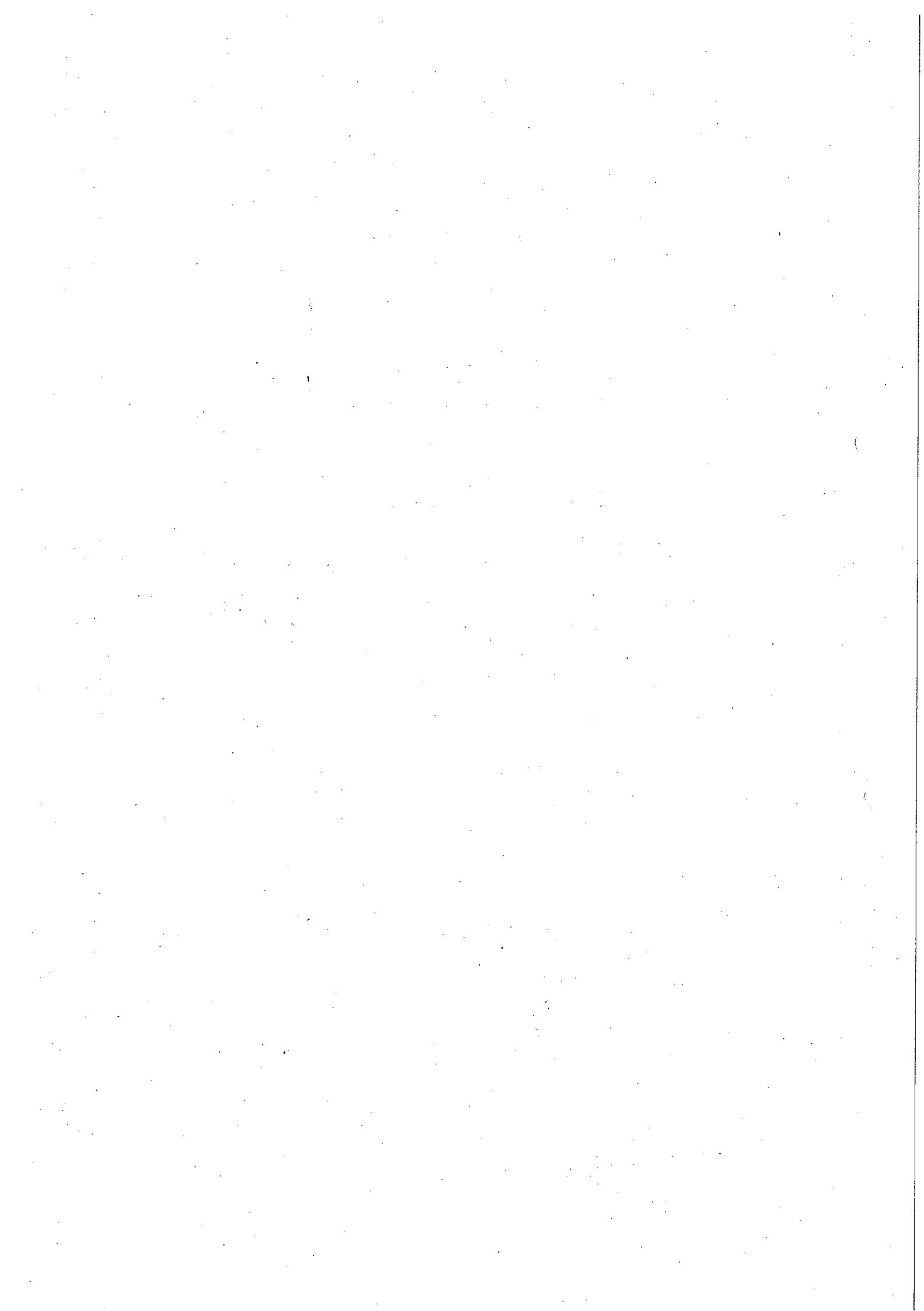
The assumptions made by Savills in calculating these figures have been based on rents towards the upper level of the market rents for this location. The rents vary considerably and those closer to the tube and with a SE1 postcode tend to be higher, in addition those with a view generally attract a higher level of rent. The methodology appears to be reasonable and the figures adopted are in line with what I would anticipate.

The effect on the IRR is approximately 0.5%.

The revised affordable appraisals reflect the following:

Shared ownership:	50% at LBS income thresholds:	£[REDACTED] per sq.ft
	50% at GLA income thresholds:	£[REDACTED] per sq.ft
Affordable Rent:	1 & 2 Beds at 50% of Market Rent:	£[REDACTED] per sq.ft
	3 Beds at Rent Caps:	£[REDACTED] per sq.ft

In addition to the revised affordable housing calculation I also understand that there have been some small variations to the scheme these are reflected in the latest version of the Financial Model that has been provided and is reflected in the revised scenario test shown below. The implications of this change on the Financial Model appear to equate to around 0.07% so the impact is minimal.



Scenario Testing

Scenarios	Incorporating GLA Policy AH Figure										Southwark/Affordable Housing Figures				
	LL Growth					DVS Growth					LL Growth			DVS Growth	
	LL Fees	DVS Fees	LL Fees	DVS Fees	AP	EUV	AP	EUV	AP	DVS Fees	AP	EUV	AP	DVS Fees	
INPUTS															
Residential Costs	0.00%	0.00%	0.00%	0.00%	(2.50%)	(2.50%)	(2.50%)	(2.50%)	(2.50%)	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Finance	7.50%	7.50%	7.50%	7.50%						7.50%	7.50%	7.50%	7.50%	7.50%	7.50%
Land Value	£48.0m	£48.0m	£48.0m	£48.0m						£48.0m	£48.0m	£48.0m	£48.0m	£48.0m	£48.0m
CIL	£9.04m	£9.04m	£9.04m	£9.04m	Base +2%	DVS	DVS	DVS	Base +2%	£9.04m	£9.04m	£9.04m	£9.04m	£9.04m	£9.04m
Escalation	25%	25%	25%	25%						25%	25%	25%	25%	25%	25%
Affordable %															
OUTPUTS			1	2	3	4	5	6	7	8	9	10	11		

AP - Acquisition Costs

9. FINAL CONCLUSION AND RECOMMENDATION

The approach adopted by Lend Lease is a robust approach to try and provide a deliverable development. The scheme on a current cost basis is clearly unviable and would not be built with this level of Affordable Housing, however, the applicant has recognised that it would not be acceptable for the scheme to come forward with no affordable housing.

The approach adopted is not without its faults, a growth approach introduces an element of forecasting which is almost impossible to predict with any element of certainty, however, it is possible to take a view on how realistic the assumptions are and review how the property market has behaved in the past over an extended period to see whether there is a probability that the assumptions are reasonable.

Whilst I do not consider that the lend lease growth profile is totally unreasonable I do think the initial growth maybe higher and then revert to a more regular growth pattern with no regeneration effect once a second-hand market is established.

The sales profiles adopted by Lend Lease are fairly aggressive and this results in a relatively short development period for a project of this nature, however, if the timescale was to be stretched this would impact on the IRR and also increase the finance costs of the scheme.

I do not consider it is possible to agree all aspects of the financial model, however, many of the assumptions have been agreed but these still results in a profit gap both from the applicant's perspective and in the view of DVS.

It is my view that the profit gap is circa £65 million this is reduced to around £30 million with the adoption of the EUV rather than the acquisition price; this is based on an IRR of 17.5% which should be an acceptable benchmark for this scheme to be funded.

The applicant currently believes there is a profit gap of circa £ [REDACTED] million; however this figures exclude a significant Development Management Fee and Project Management Fee that they will be in receipt of which are included in their Financial Model and is based on a the crude profit on cost approach.

There have been various other discussions which potentially could impact on viability; car parking was one topic, as I understand there is a wish for a car free environment.

There are a number of arguments for and against the provision of car parking, the actual value derived from the sale is going to be a fairly small proportion of the final gross development value but the impact on sales rates could be significant for certain accommodation types. The impact on the one and two bed units is likely to be less significant in an inner city location than in a suburban location, however, for family housing it will potentially be more of an issue. The availability of properties which have parking will potentially be more attractive even were alternative schemes exist such as car clubs, as it limits choice and is not always available to meet the demands of family requirements.

The key aspect of any phase development is the cashflow and the timing of non construction elements can impact on the viability, particular prior to the revenue stream commencing. Section 106 payments added to high initial infrastructure and site preparation costs can have cashflow implications and necessitate the need for additional finance, timing the payments towards the end of the construction period or after significant revenue has been received. This will be advantageous to the developer but it is not always appropriate as the development will once partly occupied, starts to create a burden on the public purse which will need to be addressed. Ideally it would be advantageous to have a phased payment process linked to delivery.

The main problem in commencing a development at the current time is the availability of finance and if there is uncertainty this will be harder to obtain. Where I have undertaken outturn assessments in the past the aim was to get an acceptable level of affordable housing but would enable the development to be delivered.

The applicant's offer to commence development with a fixed 25% affordable housing provision represents a reasonable offer but does need some safeguarding.

The scheme as currently proposed does not provide a policy compliant affordable housing provision and I understand the desire to try and protect that policy with the use of clawback arrangements if the scheme exceeds expectations, however, the provision of a clawback arrangements introduces an element of uncertainty and could affect the ability to obtain funding and consequently delivery of the scheme. The current scheme is already providing significantly more affordable housing than it can afford on a current cost basis.

The alternative approach is to look at the current cost and review at each phase but from a viability perspective this is likely to produce less affordable in the short term and will

probably hinder delivery although could provide better returns at the end of the scheme but this by no means guaranteed.

As I have already stated the applicant's offer to commence development with a fixed 25% affordable housing provision is reasonable. However, to safeguard against the developer waiting for a significant improvement in the market prior to commencement there does need to be a review mechanism of some description. Therefore in order to ensure the development is delivered in an agreed acceptable timeframe a viability review should be built in if this is not achieved. In terms of how this should work it will be necessary to agree an appropriate timetable with certain tolerances to allow for unforeseen problems and various trigger points.

In terms of the trigger points I do not think this should be tied to commencement of a particular stage as this does not necessarily guarantee delivery therefore I would recommend that the trigger points are more appropriately tied to the delivery of the number of units or phases.

This approach is preferable to claw-back as it gives the developer certainty and it is within their control. It should be noted that the RICS guidance does not recommend claw-back provisions.

It is assumed that if the proposal were to change significantly this would also enable a review of the viability.

I trust that the viability review is clear. You may have queries on a number of the issues I have raised, and I would be happy to discuss these.

Chris Kench MRICS

Registered Valuer

Principal Surveyor

DVS

Appendix 1 - Assessment of Residential Analysis

Savills have provided a report into proposed Residential Values as Appendix 12 to their report.

They conclude that private sale values on the site should be:

£500 - £650 per sq ft for the low rise blocks

£600 - £700 per sq ft for high rise blocks

Further concluding that an average for the whole scheme be in the order of £600 per sq ft.

It is acknowledged by DVS the difficulty in accurately valuing the residential market sale values for this scheme due to the scale and impact the scheme will have on this deprived inner city area, which in turn means that much of the local sales evidence is not comparable to what is proposed. The majority of evidence has been drawn from Elephant and Castle and developments to the south. Whilst DVS recognise that values to the north of Elephant and Castle are likely to be higher due to being in a more valuable location it does not give an idea of what may be achieved following redevelopment.

Savills have provided a range of appropriate sales evidence from new build schemes in SE1 and SE17. The best evidence due to its proximity for high rise residential is Strata. It is noted that evidence provided is all from 2010 and that DVS have seen that values have risen in the last year or so in this tower.

Strata SE1

It is likely that the recession impacted the prices that are being currently achieved. The scheme was launched prior to the recession and following the downturn many sales failed to complete and the unsold units had to be re-marketed. Whilst it would be too strong that this has blighted this development I consider it has had an impact and if an identical scheme was launched fresh today it is likely to achieve better values. I have inspected several units from the 11th to 37th floor and consider that the specification was below the standard that you would expect for a landmark tower development, this may have been driven by the impact of the recession but the kitchens and bathrooms, whilst acceptable, in the units I inspected had utilised relatively basic fittings and ceramic tiles. This point is somewhat subjective but it was an impression enhanced by signs of wear in the common parts. The fact that there are only

23 parking spaces we have been told for the whole of the development may have impacted desirability to potential purchasers.

Analysis of sales between July 2011 and the start of 2012 show an average sale price of £674 per sq ft suggesting, whilst acknowledging half of these sales are at floors 35 and above, that values have risen since sales in 2010.

Apartment	Floor	Beds	Sale date	Area / sq ft	Price	Price / sq ft
1411	14	2	21 Oct 2011	715	£392,000	£548
1505	15	2	23 Aug 2011	747	£368,500	£493
1511	15	2	24 Aug 2011	715	£400,000	£559
1708	17	2	11 Aug 2011	747	£400,000	£535
2002	20	2	09 Dec 2011	715	£415,000	£580
2403	24	1	02 Dec 2011	378	£265,000	£701
2602	26	1	01 July 2011	567	£345,000	£608
3405	34	1	07 Oct 2011	464	£310,000	£668
3506	35	1	07 Oct 2011	464	£312,000	£672
3701	37	3	09 Dec 2011	1,243	£1,125,000	£905
3705	37	1	22 Aug 2011	466	£305,000	£655
3706	37	1	22 Aug 2011	466	£305,000	£655
3801	38	3	14 Sep 2011	1,079	£820,000	£760
3804	38	2	07 Oct 2011	468	£310,000	£662
3805	38	1	07 Oct 2011	468	£315,000	£673
4103	41	1	25 Nov 2011	1,066	£553,000	£519
4105	41	3	19 Jan 2012	1,863	£1,575,000	£845
				12,631	£8,515,500	£674

Metropolis, 157 New Kent Road SE1

This five storey development just to the north of Heygate is nearing completion. The immediate surroundings are currently inauspicious, located next to a children's nursery and a row of tertiary shop units, but is likely to improve. This predominantly brick fronted building is

selling well and achieving within a few percent of asking price. Ground rents are £250 per annum for one bed and £300 per annum for two beds. All units either have a balcony or terrace.

We are aware that four units have exchanged, and all but one are under offer, of the 10 market units in this phase.

Clearly these units reflect what prices are achievable for new build low rise flats in this location where regeneration is several years away.

Address	Floor	Beds	Size (sq ft)	Price	Price per sq ft
5	2	2	800	£375,000	£469
6	2	2	822	Available	
7	2	1	553	£275,000	£497
8	2	2	781	£382,000	£489
9	3	3	1004	£475,000	£473
10	3	3	900	£440,000	£489
11	3	2	781	£385,000	£493
12	4	3	1069	£552,000	£516
13	4	2	772	£455,000	£589
15	2/3	2	915	£475,000	£519
					£504

Sadler's Court, Wilds Rents SE1

This scheme of one and two bed units has been mainly sold off plan. It is in a slightly better location due to its proximity to London Bridge but it is surrounded by a mixture of Local Authority flats and secondary commercial premises. Values for this five storey building are from high £500's to low/mid £600's, per sq ft. DVS consider that although the area is mixed it's value is driven by that it is only a 12 minute walk from London Bridge.

Interestingly eight units were sold to an investor where the discount from asking price to price paid was 84.7 % where as non bulk transactions all achieved at least 95% of asking price.

Printworks, Amelia Street SE17 3BY

DVS requested all the sales date from Printworks, an eight storey development in SE17. Sales since 2010, according to Savills, had a total weighted average across the scheme equating to £450 per sq ft.

70 Great Suffolk Street SE1 0BL

Flat 4, is a 2 bed 2 bath unit of 787 sq ft in a new block that sold in February 2012 for £500,000 equating to £635 per sq ft. This evidence reflects the enhanced prices that are achieved by a unit that lies 0.7 miles (a 15 minute walk) directly to the north.

Savills then consider other regeneration areas within London.

Vauxhall / Nine Elms

It is noted that beyond the immediate environs of Vauxhall, the transport links are currently not good considering its central location. Riverside and river facing units in particular will achieve premiums not achievable at Elephant and Castle. What may drive value in these locations in the future is the redevelopment of Nine Elms including Battersea Power Station and the extension to the Northern Line to provide nearby access to the Underground network.

Riverlight (Berkeley)

(Assuming not waterfront – waterfront) - £600 - £900 per sq ft

St. George's Wharf waterfront (St. George) - £950 per sq ft

St. George's Wharf not waterfront (St. George) - £600 per sq ft

Viridian (Barratt) - £500 per sq ft

This Space (Mount Anvil) – £500 per sq ft

Bermondsey Spa

This 50 acre regeneration area, due to deliver circa 2,000 new homes, lies one and half miles to the east of Elephant and Castle. One of the most recent developments has been the Parker Building that was launched in Asia in the summer of 2011 and the units have been

selling quickly (2 per week) with no incentives. The development has been built by Hyde Housing Association creating 319 new units of which 87 are private, 131 social rented and 101 are intermediate tenure. Forty eight of the market units have been sold to date. All have balconies in this nine storey building.

The location has not got quite as good transport links as Elephant and Castle but Southwark Underground station (Jubilee Line) is only a few minutes walk.

The Parker Building, Bermondsey Spa, Jamaica Road, London SE16 4EF

Recent sales as at 26.04.12

One bed apartments

Address	Floor	Aspect	Size (sq ft)	Price	Price per sq ft
74	5th	Eastside facing AH block	500	£285,000	£570
19	4th	North West facing, Abbey Street	499	£300,000	£601
116	7th	Eastside facing AH block	497	£300,000	£604
42	7th	South West point of block	575	£310,000	£539
37	7th	North West facing, Abbey Street	499	£320,000	£641

Two bed apartments

Address	Floor	Aspect	Size (sq ft)	Price	Price per sq ft
22	4 th	Jamaica Road	741	£390,000	£526
108	6 th	South East corner fronting Jamaica Road	791	Quoting £400,000	£506
79	6 th	South West facing	778	£400,000	£514
112	6 th	Jamaica Road	803	£405,000	£504
40	7th	Jamaica Road	741	£410,000	£553

The three bed units are to be released shortly at a price equating to circa £600 per sq ft. Undercroft parking is priced at £15,000 per space. Ground rents are £150 per annum for one

beds, £250 per annum for two beds and £350 per annum for three beds. Service Charge for one beds are £100 per month, two beds are £150 per month.

The Tanyard, George Row, Bermondsey SE16

A small development of 17 one and two bed flats by Linden Homes located on the north side of Jamaica Road, on the corner of George Row. All but two units have sold in this six storey apartment block at close to asking price. There is no parking.

A 2 bed unit measuring 727 sq ft, benefiting from a large balcony, on the 6th floors with good views sold for £485,000 equating to £667 per sq ft. Whilst this was the highest sale price the majority of units archived over £600 per sq ft with the average asking price equating to £623 per sq ft.

DVS have read Savills pricing rationale and, as far as can be gathered from the information provided, agree with it's position. The statement "However in summary we expect new build sales values at Elephant and Castle to slightly exceed current values" strikes of being overly pessimistic.

Bulk sale discounts have been shown to be between 10 to 15% on capital values at Sadler's Court not the 15% to 20% Savills have suggested.

Savills have suggested ground rents should be as follows:

Studio	£250
One bed	£300
Two bed	£375
Three bed	£500

They have provided evidence from a range of developments and DVS consider their suggestion falls within a range we consider acceptable for this development.

Conclusion

It is DVS opinion that Savills pricing proposals is broadly reasonable, particularly given the lack of strong evidence. DVS consider that the low and mid rise average values are broadly correct but question whether the tower buildings averages are pessimistic. DVS consider that the evidence from the Strata tower is slightly misleading due to the specification, maintenance and marketing history.

Whilst the provision of a large number of towers in close proximity does call into question whether the premium that this type of accommodation provides will lose its exclusivity (and therefore value) and the impact of restricted views. Nonetheless there will be some stunning views from many apartments, for instance overlooking the Shard at London Bridge as well as more established views of Canary Wharf, the City and the West End. We would not be surprised if significantly better values are not achieved in this element of the scheme.

Therefore, we have considered the impact an overall increase of 5% would have on the development viability.

Appendix 2 - Development Cost Analysis

Glenn Ramos - 13 July 2012

1. Introduction

1.1 The purpose of this report is to provide a review of the estimated construction costs supplied for the proposed mixed use development at The Heygate Estate – Elephant and Castle, London.

1.2 Briefly, the proposed development comprises of (but not limited to):

- Demolition of existing structures not required
- Provision of 2,462 residential units
- Provision of shell only retail, commercial, leisure and business use
- Basement car parking
- All associated infrastructure, external and builder's works

The site is sub divided into 12 individual plots (H1-H7, H10, H11a, H11b, H12 and H13) and will be built over 5 Phases (Phase 2 to Phase 6).

1.3 Savills Viability Assessment, dated 9 May 2012 and in particular the Gardiner and Theobald (G&T) Proposed Build Cost Estimate (Appendix 16) was the main document used with a specific view to make comments on the construction costs associated with the said development.

1.4 A meeting was held on the 20th June 2012 at G&T offices to go through the cost estimate. Additional information was received subsequently as a result of this meeting.

2. Commentary on G&T Initial Indicative High Level Cost Plan

2.1. It is assumed that for the purposes of this exercise that overall Gross External Area (GEA) provided at 277,842m² is correct and measured in accordance of RICS Code of Measuring Practice, 6th Edition, September 2007.

2.2. In order to arrive at an equivalent Gross Internal Area (GIA), for the purposes of build cost calculation, it is assumed that the net to gross ratio is 93%. Therefore effective GIA would equate to 258,393m².

2.3. For avoidance of doubt, the build cost that I will be comparing against is circa £ [REDACTED]. This was based on the following information:

- Buildings [REDACTED]
- Infrastructure and Public Realm [REDACTED]

TOTAL at 1Q2011 Prices

[REDACTED]

- 2.4. It appears that information from the planning application website such as Design and Access Statement, Environmental Statement, Landscaping and Open Space Statement, Planning Statement, Transport Statement, etc. were not considered by G&T as forming the basis of the estimate. Whilst this may or may not impact on costs, confirmation is required whether these documents were considered.
- 2.5. Additional information is required as we do not appear to have a copy of the Illustrative Master Plan Pack and Eon Report from the cost plan basis of estimate.
- 2.6. Please note that allowance to comply with Code for Sustainable Homes 4 was included in the cost plan. This was however built into the rates for the residential and was not identifiable separately.
- 2.7. Confirmation is required whether extra over costs to comply with BREEAM rating excellent is a requirement for non residential uses and whether allowance has been made in the cost plan.
- 2.8. An allowance of circa £ [REDACTED] or £ [REDACTED]/residential unit has been included in the cost plan to cover for Zero Carbon Homes 'Fabric Energy Efficiency Standard'. Confirmation is required whether this is a planning condition.
- 2.9. Please note that costs are current at 1Q2012 pricing levels with no allowance for further inflation. This should be adjusted to reflect current costs at 3Q2012.
- 2.10. It is assumed at this stage that non residential building uses i.e. retail, business, commercial, leisure, etc will be constructed to 'Shell and Core' only.
- 2.11. Assumptions and exclusions need to be reviewed to ensure monies are allowed elsewhere in the development appraisal whenever required.
- 2.12. Additional information was received subsequent to the meeting on 20th June 2012:

- Public Realm Drawing and Information
- Arup Infrastructure Plans
- Development Programme
- Extract from Management Board Papers re: HV Connection Proposal for Heygate and Rodney Road
- Proposed Accommodation Schedule
- Indicative Plot Plan Footprints
- E&C Masterplan Area Schedule (277,842m² GEA)
- G&T Residential Benchmarking Exercise
- Evidence based information regarding Utilities Diversions, On Site and Off Site Reinforcements

2.13. It is assumed for the purposes of this exercise that quantities provided for all the infrastructure cost headings were measured correctly. These had not been validated in full detail with G&T at this stage.

2.14. Please note that allowances were provided for surveys and reports such as topographic surveys, contamination surveys, asbestos surveys, etc which amounted to circa £ [REDACTED] These were left included in the assessment. Potential double counting may arise in the development appraisal.

2.15. Whilst documentary evidence was provided for Gas Diversions, no information were received to validate the diversion costs for drainage, water, BT, Virgin Media and electrical. Kindly provide.

2.16. Please note that no cost advice was sought for On Site Networks from Utilities Companies due to the early state of development.

2.17. Clarification is required whether the cost for Diversion Works, Off Site Reinforcement and On Site Networks included an element of Consultant's Fees.

2.18. The Arup Infrastructure Plans showed the services network to include Phase 1 which is excluded from this development appraisal. Confirmation is required whether allowances were included in the cost plan to include for Phase 1.

2.19. Please note allowances were provided for Highways outside the red line planning application boundary. Total cost amounts to circa £ [REDACTED] for Highway works to

Rodney Road, New Kent Road, Walworth Road and Rodney Place. These were left included in the assessment. Potential double counting may arise in the development appraisal.

2.20. Please note that allowances were provided for Junction Works to Phase 1 amounting to circa £ [REDACTED]. These should be excluded from the assessment.

2.21. Please note that the Public Realm Drawing included hard and soft landscaping to Phase 1. Confirmation is required whether allowances were included in the cost plan to include for Phase 1.

2.22. Allowances were provided for off site tree works amounting to circa £ [REDACTED]m. Confirmation is required whether these form part of the overall scope of works. These were left included in the assessment. Potential double counting may arise in the development appraisal.

2.23. Provisional Sum allowances should be reviewed once further design development information is received such as:

- Allowance for nursery facility - £ [REDACTED]k
- Allowance for protection of existing trees - £ [REDACTED]k
- Allowance for maintenance nursery - £ [REDACTED]k
- Allow bulk earthworks, storage costs crushed concrete - £ [REDACTED]k
- Allowance for water feature - £ [REDACTED]k

2.24. Clarification is required whether there was an element of double counting in the cost plan. For example, an allowance of £ [REDACTED]k was included for tree protection in the demolition section. Further allowance of £ [REDACTED]k was included for protection to existing trees under site enabling works. A further allowance of £ [REDACTED]m was included for tree protection works under the public realm section. Based on the Arboricultural Report as indicated in the Design and Access Statement, there were only 406nr existing tree on site. Confirmation is required if this document was utilised by G&T in preparing the cost plan.

2.25. Confirmation is required whether no allowances were made in the cost plan in relation to Oakmayne Plaza Development.

- 2.26. There was no programme provided in relation to how infrastructure works will be carried out. It is assumed that a lot of upfront costs will be carried out to provide infrastructure costs prior to or whilst Phase 1 works is carried out. Kindly provide.
- 2.27. It is assumed that no market testing exercise was carried out at this stage to validate the residential build costs.

3. Construction Costs

- 3.1. Please find attached an order of cost estimate for the proposed development. Overall construction costs include preliminaries, overheads and profit, contingency, external works including infrastructure, and sustainability. It excludes VAT, Fees, S106 contributions, etc.
- 3.2. The assessment was based on the effective GIA as assumed. Any changes to the areas will have an impact on the overall construction costs.
- 3.3. DVS assessment utilises schemes of similar nature adjusted for abnormalities, location and time factors.

4. On Costs (Preliminaries, Overheads and Profit, Contingency)

- 4.1. Preliminaries vary depending on the value of the works to be carried out. Generally, preliminaries appear reasonable commensurate with the level of information available and in comparison with other schemes of similar nature.
- 4.2. Overheads and profit at 10% - 12% may appear on the upper end of the scale.
- 4.3. Please note that no allowance was made for contingency in the assessment. It is expected that 10% is a reasonable assessment at this stage of development.

A study of preliminaries, overheads and profit can be achieved from the benchmarking exercise provided by G&T.

5. Professional Fees

- 5.1. Professional Fees are excluded from this assessment. It is expected that construction consultant fees would fall within the region of 8% - 12%.

6. Conclusions

- 6.1. The assessment assumed that what was provided for in the G&T cost plan is the overall scope of works required. If confirmation is received that allowances were made for Phase 1 works and anything outside the boundary should not be considered, obviously these should effectively be taken out from both assessments.
- 6.2. Where items can not be validated due to the absence of further evidence by way of reports, back up calculations, etc. these figures remain in the DVS assessment.
- 6.3. The original submission amounts to circa £ [REDACTED]. Adjusting this to reflect current cost at 3Q2012 utilising BCIS Tender Price Indices for the purposes of this exercise would equate to circa £ [REDACTED].
- 6.4. The current DVS order of cost estimate is circa £ [REDACTED], £ [REDACTED] (5%) less than G&T's adjusted figures at 3Q2012. The difference as being not unreasonable at this stage and design of development.
- 6.5. A letter was provided by G&T as part of Savills Viability Assessment (Appendix 17) which suggests that potential savings can be achieved by 2% to 3%.
- 6.6. If a saving is applied utilising 2.5% (average), then the DVS order of cost assessment is circa £ [REDACTED] (2%) less than G&T's adjusted figures at 3Q2012. The difference still being not unreasonable at this stage and design of development.
- 6.7. Benchmarking exercise was provided by G&T to validate the overall cost per m² rate provided for this scheme. It is assumed that the benchmarking is adjusted to cost and time factors.
- 6.8. It is assumed that the rates adopted would cover the likely specification for this scheme commensurate with the sales / values.

Cost Analysis Summary

Proposed Mixed Use Development
Land at Elephant and Castle, London SE1 6TE
Summary

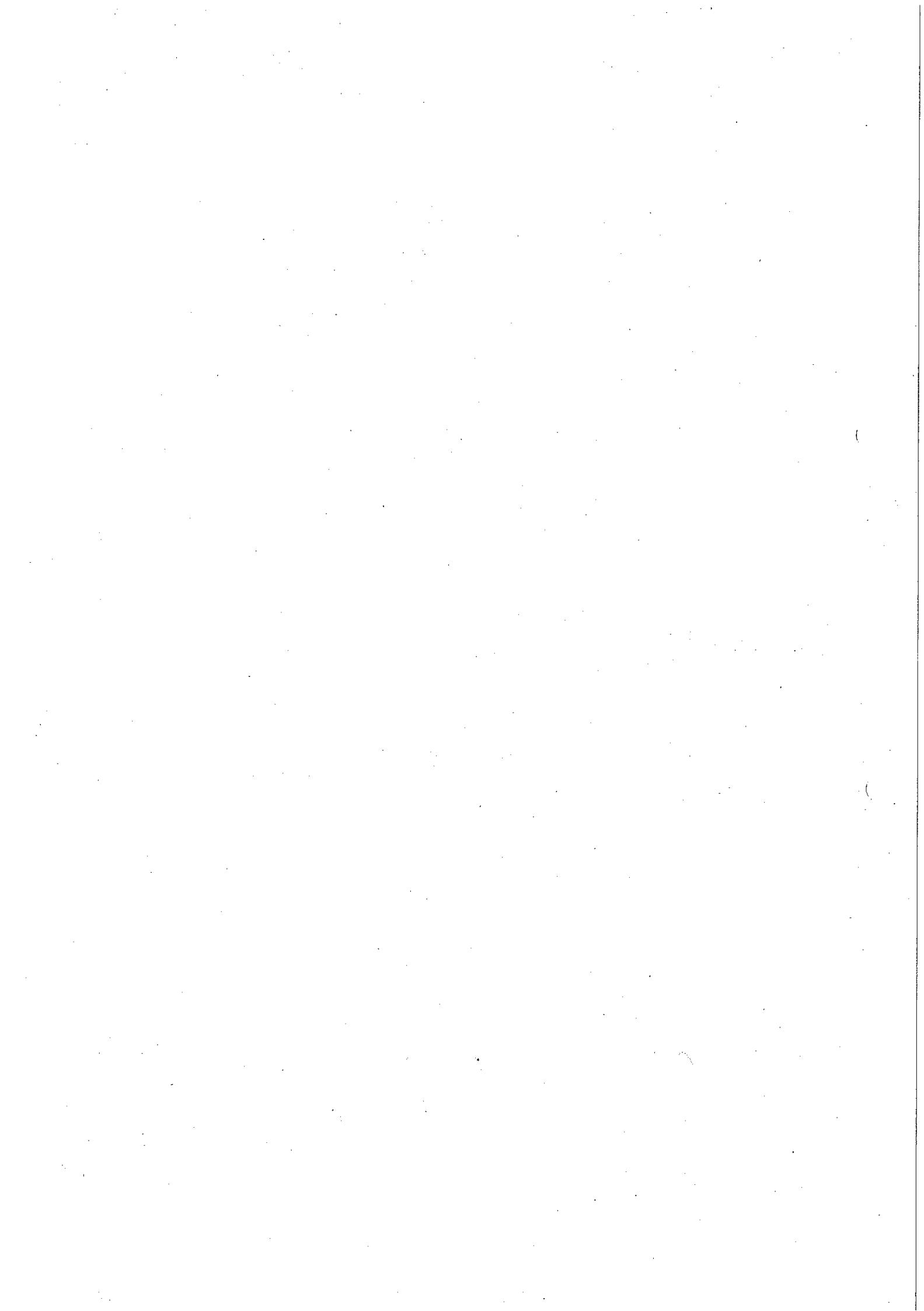
Description	Submitted Costs	Adjusted Costs	DVS	Difference	% Difference
Build Costs					
Residential			461,383,143		
Retail			18,613,930		
Café / Restaurant			3,616,693		
Commercial Business Use			9,191,820		
Leisure			1,937,794		
Community			3,767,323		
Energy Centre			1,582,039		
Basement Car Park			18,794,742		
EO Code for Sustainable Homes 4	In	In	Included above		
EO uplift for Zero Carbon Homes			5,714,322		
EO Landscaping to Roof			11,225,955		
Infrastructure Works					
Demolition			12,636,035		
Bulk Earthworks			4,521,266		
Site Logistics			1,986,802		
Site Enabling Works			2,686,244		
Utilities Diversions			3,380,134		
Off - Site Reinforcement			6,045,387		
On - Site Reinforcement			9,773,665		
Plot Connections			4,523,119		
Plot Connections Esco			4,081,594		
Highways			7,067,727		
Public Realm			22,267,775		
Fees			excluded		
Contingency			excluded		
Estimated Construction Cost at 3Q2012			614,797,530		
Rate per m ²			2,379		
Rate per ft ²			221		

Proposed Heygate Estate Refurbishment
Land at Elephant and Castle, London SE1 6TE
Summary

Description	Submitted Costs	DVS	Difference	% Difference
Residential				
Internal Refurb to building	29,060,553			
Soft Strip Works - Buildings	2,362,070			
Soft Strip Works - Garages	325,019			
Roof Works	4,214,668			
Replace Garage Doors	421,027			
External Repairs to walkways and balconies	1,092,456			
Works to envelope	4,440,770			
Other Areas				
Boiler House	54,435			
Retail Units	513,682			
Petrol Station	23,621			
Doctors Surgery	171,327			
Community Centre	171,327			
Housing Office	209,001			
External Works				
CCTV - new systems	598,000			
Allowance for supplementing existing soft landscaping	1,352,694			
Allowance for repairs to hard surfaces	468,593			
Allowance for repairs to ramp expansion joints	239,200			
Allowance for re-surfacing of estate roads - wearing course only	511,499			
Allowance for repairs to external lighting attached to buildings	239,200			
Allowance for additional external lighting to public realm	2,705,388			
Contingency	2,458,726			
Estimated Construction Cost at 3Q2012	51,633,266			
Rate per m ²		609		
Rate per ft ²		57		

Costs are current at 3Q2012. No movement in BCIS TPI Indices from 2Q2012 to 3Q2012.

Appendix 3 – EUV Valuation



Valuation Office Agency

Development Appraisal

Appendix 3

Refurbishment of Existing Estate

**Heygate Estate
Elephant & Castle
London SE17**

Report Date 13/07/2012

TIMESCALE & ASSUMPTIONS

VALUATION OFFICE AGENCY

Appendix 3

Refurbishment of Existing Estate

Timescale (Duration in months)

Project commences Jun 2012

Phase 1

Stage Name	Duration	Start Date	End Date	Anchored To	Aligner	Offset
Phase Start		Jun 2012				
Pre-Construction	3	Jun 2012	Aug 2012	Purchase	End	0
Construction	36	Sep 2012	Aug 2015	Pre-Construction	End	0
Sale	36	Sep 2013	Aug 2016	(None)	Start	0
Phase End			Aug 2016			
Phase Length	51					

Phase 2

Stage Name	Duration	Start Date	End Date	Anchored To	Aligner	Offset
Phase Start		Jun 2012				
Pre-Construction	3	Jun 2012	Aug 2012	Purchase	End	0
Construction	36	Sep 2012	Aug 2015	Pre-Construction	End	0
Sale	36	Sep 2013	Aug 2016	(None)	Start	0
Phase End			Aug 2016			
Phase Length	51					

Project Length **51** (Merged Phases - Includes Exit Period)

Assumptions

Expenditure

- Professional Fees are based on Construction
(Manual relations applied to some Professional Fees)
- Purchaser's Costs are based on Gross Capitalisation
- Purchaser's Costs Deducted from Sale (Not added to Cost)
- Sales Fees are based on Net Capitalisation
- Sales Fees Added to Cost (Not deducted from Sale)

Receipts

- | | |
|--|------------------------------|
| Show tenant's true income stream | On |
| Offset Income against development costs | Off |
| Rent payment cycle | Quarterly (Adv) |
| Apply rent payment cycle to all tenants | On |
| Renewal Void and Rent Free apply to first renewal only | Off |
| Initial Yield Valuation Method | Off |
| Default Capitalisation Yield | 0.0000% |
| Apply Default Capitalisation to All Tenants | Off |
| Default stage for Sale Date | Off |
| Align end of income stream to Sale Date | Off |
| Apply align end of income stream to all tenants | On |
| When the Capital Value is modified in the cash flow | Recalculate the Yield |
| Valuation Tables are | Annually in Arrears |
| Rent Free method | Defer start of Tenant's Rent |

Finance

- | | |
|---|-----------------------|
| Financing Method | Basic (Interest Sets) |
| Interest Compounding Period | Quarterly |
| Interest Charging Period | Monthly |
| Nominal rates of interest used | |
| Calculate interest on Payments/Receipts in final period | Off |
| Include interest and Finance Fees in IRR Calculations | Off |

TIMESCALE & ASSUMPTIONS**VALUATION OFFICE AGENCY****Appendix 3****Refurbishment of Existing Estate****Assumptions**

Automatic Inter-account transfers	Off
Manual Finance Rate for Profit Erosion	Off
Calculation	
Site Payments	In Arrears
Other Payments	In Arrears
Negative Land	In Arrears
Receipts	In Advance
Initial IRR Guess Rate	8.00%
Minimum IRR	-100%
Maximum IRR	99999%
Manual Discount Rate	Off
IRR Tolerance	0.001000
Letting and Rent Review Fees are calculated on	Net of Deductions
Development Yield and Rent Cover are calculated on	Rent at Sale Date(s)
Include Tenants with no Capital Value	On
Include Turnover Rent	Off
Net of Non-Recoverable costs	On
Net of Ground Rent deductions	On
Net of Rent Additions/Costs	On
Value Added Tax	
Global VAT Rate	0.00%
Global Recovery Rate	0.00%
Recovery Cycle every	2 months
1st Recovery Month	2 (Jul 2012)
VAT Calculations in Cash Flow	On

Residual

Land Cost Mode	Residualised Land Value
Multi-Phasing	Separate Land Residual for each phase
Target Type	Profit on Cost

Phase Number	Target Value	Locked Value	Treat Neg Land as Revenue
Phase 1	25.00%	No	No
Phase 2	6.00%	No	No

Distribution

Construction Payments are paid on	S-Curve
Sales Receipts are paid on	Single curve
Sales Deposits are paid on	Monthly curve

Interest Sets**Interest Set 1**

Debit Rate	Credit Rate	Months	Start Date
7.000%	2.500%	Perpetuity	Jun 2012

Loan Set 1

Debit Rate	Credit Rate	Months	Start Date
0.000%	0.000%	Perpetuity	Jun 2012

TIMESCALE & ASSUMPTIONS**VALUATION OFFICE AGENCY****Appendix 3
Refurbishment of Existing Estate****Assumptions****Inflation and Growth****Growth Sets****Growth Set 1**

Inflation/Growth for this set is calculated in arrears
This set is not stepped

	Rate	Months	Start Date
	0.000%	Perpetuity	Jun 2012

Inflation Sets**Inflation Set 1**

Inflation/Growth for this set is calculated in arrears
This set is not stepped

	Rate	Months	Start Date
	0.000%	Perpetuity	Jun 2012

APPRAISAL SUMMARY

VALUATION OFFICE AGENCY

Appendix 3 Refurbishment of Existing Estate

Summary Appraisal for Merged Phases 1 & 2

REVENUE

Sales Valuation	ft ²	Rate ft ²	Gross Sales	
Private 1 Bed	45,983	£328.82	15,120,260	
Private 2 Bed	38,750	£340.56	13,196,608	
Private 3 Bed	12,744	£313.68	3,997,635	
Private 4 Bed	7,750	£288.96	2,239,422	
Affordable	567,968	£104.58	59,398,693	
Totals	<u>673,196</u>		<u>93,952,618</u>	93,952,618

Rental Area Summary

	Units	Unit Amount	Gross MRV
Ground rents 1 bed	89 units at	£200	17,800
Ground rents 2 bed	60 units at	£250	15,000
Ground rents 3 & 4 bed	24 units at	£300	7,200
Garages	560 units at	£585	327,600
Totals			<u>367,600</u>

	ft ²	Rate ft ²	Gross MRV
Retail	17,567	£13.50	237,155
Petrol Station	808	£13.49	10,901
Community Hall	5,551	£7.50	41,633
Doctors Surgery	6,168	£15.00	92,520
Housing Office	6,433	£7.50	48,248
Totals	<u>36,527</u>		<u>430,457</u>

Investment Valuation

Ground rents 1 bed					
Current Rent	17,800	YP @	6.0000%	16.6667	296,667
Ground rents 2 bed					
Current Rent	15,000	YP @	6.0000%	16.6667	250,000
Ground rents 3 & 4 bed					
Current Rent	7,200	YP @	6.0000%	16.6667	120,000
Retail					
Market Rent	237,155	YP @	8.0000%	12.5000	
(0yrs 7mths Rent Free)		PV 0yrs 7mths @	8.0000%	0.9561	2,834,295
Petrol Station					
Market Rent	10,901	YP @	8.0000%	12.5000	
(1yr 1mth Rent Free)		PV 1yr 1mth @	8.0000%	0.9200	125,362
Community Hall					
Current Rent	41,633	YP @	10.0000%	10.0000	416,330
Doctors Surgery					
Market Rent	92,520	YP @	7.0000%	14.2857	
(1yr 1mth Rent Free)		PV 1yr 1mth @	7.0000%	0.9293	1,228,302
Garages					
Market Rent	327,600	YP @	8.0000%	12.5000	
(0yrs 1mths Rent Free)		PV 0yrs 1mths @	8.0000%	0.9936	4,068,821
Housing Office					
Current Rent	48,248	YP @	10.0000%	10.0000	482,480
					9,822,258

GROSS DEVELOPMENT VALUE **103,774,876**

Income from Tenants

Ground rents 1 bed	16,317
Ground rents 2 bed	13,750
Ground rents 3 & 4 bed	6,600

36,667

103,811,543

APPRAISAL SUMMARY**VALUATION OFFICE AGENCY**
Appendix 3
Refurbishment of Existing Estate
OUTLAY**ACQUISITION COSTS**

Residualised Price		26,444,833
Stamp Duty	4.00%	1,057,793
Agent Fee	1.00%	264,448
Legal Fee	0.35%	92,557
		27,859,632

CONSTRUCTION COSTS

Construction	Units	Unit Amount	Cost
Garages	560 units at ft ²	£752	421,027
Retail	18,492	£27.78	513,682
Petrol Station	850	£27.79	23,621
Community Hall	6,168	£27.78	171,327
Doctors Surgery	6,168	£27.78	171,327
Housing Office	7,148	£29.24	209,001
Private 1 Bed	58,119	£42.27	2,456,670
Private 2 Bed	48,976	£42.27	2,070,228
Private 3 Bed	16,108	£42.27	680,875
Private 4 Bed	9,795	£42.27	414,045
Affordable	717,856	£42.27	30,343,791
Totals	<u>889,680</u>		<u>37,054,567</u>
Contingency		5.00%	2,458,896
Road/Site Works			6,114,574
			8,573,470

Other Construction

Boiler House		54,535
Walkways		1,092,456
Works to envelope		4,440,770
		5,587,761

PROFESSIONAL FEES

Architect	6.00%	2,728,414
		2,728,414

MARKETING & LETTING

Marketing	1.00%	345,539
Letting Agent Fee	10.00%	79,806
Letting Legal Fee	5.00%	39,903
		465,248

DISPOSAL FEES

Sales Agent Fee	1.25%	554,702
Sales Legal Fee	0.25%	259,437
		814,139

FINANCE

Multiple Finance Rates Used (See Assumptions)	
Total Finance Cost	8,013,220

TOTAL COSTS

91,517,478

PROFIT

12,294,064

Performance Measures

Profit on Cost%	13.43%
Profit on GDV%	11.85%
Profit on NDV%	11.85%
Development Yield% (on Rent)	0.87%
Equivalent Yield% (Nominal)	7.92%

APPRAISAL SUMMARY**VALUATION OFFICE AGENCY****Appendix 3****Refurbishment of Existing Estate**

Equivalent Yield% (True)	7.92%
Gross Initial Yield%	8.13%
Net Initial Yield%	8.13%
IRR	14.71%
Rent Cover	15 yrs 5 mths
Profit Erosion (finance rate 7.000%)	1 yr 10 mths

RENT & SALES SCHEDULE
VALUATION OFFICE AGENCY
**Appendix 3
Refurbishment of Existing Estate
RENT AND CAPITALISATION**

Areas (Sq Feet)	Units	Area/Unit ft²	Total Net Area ft²	Rent £ ft²	Gross MRV £ pa	Adjustment	Net MRV £ pa	Yield%	YP	Net Capital Value
Ground rents 1 bed	89	0	0	0.00	17,800	0	17,800	6.00	16,8867	296,667
Ground rents 2 bed	60	0	0	0.00	15,000	0	15,000	6.00	16,8867	250,000
Ground rents 3 & 4 bed	24	0	0	0.00	7,200	0	7,200	6.00	16,8867	120,000
Retail	1	17,567	17,567	13.50	237,155	0	237,155	8.00	12,5000	§ 2,834,295
Petrol Station	1	808	808	13.49	10,901	0	10,901	8.00	12,5000	§ 125,382
Community Hall	1	5,551	5,551	7.50	41,633	0	41,633	10.00	10,0000	416,330
Doctors Surgery	1	6,168	6,168	15.00	92,520	0	92,520	7.00	14,2857	§ 1,228,302
Garages	660	0	0	0.00	327,600	0	327,600	8.00	12,5000	§ 4,068,621
Housing Office	1	6,433	6,433	7.50	48,248	0	48,248	10.00	10,0000	482,480
Totals			36,527		798,057	0	798,057			8,822,258

§ Rent Free Periods granted to these tenants. See full schedule for extra detail.

SALES

Areas (Sq Feet)	Units	Area/Unit ft²	Total Net Area ft²	Sales £ ppa	Per Unit £ pa	Gross Sales £ pa	Adjustment	Net Sales £ pa
Private 1 Bed	89	517	45,983	328.82	169,891	15,120,260	0	15,120,260
Private 2 Bed	60	646	38,750	340.56	219,943	13,196,608	0	13,196,608
Private 3 Bed	16	797	12,744	313.68	249,852	3,997,635	0	3,997,635
Private 4 Bed	8	969	7,750	288.96	279,928	2,239,422	0	2,239,422
Totals			105,228			34,553,925	0	34,553,925
Affordable	934	608	567,968	104.58	63,598	59,398,693	0	59,398,693