GL Hearn

Financial Viability Report

Economic Viability Analysis & Justification in Respect of:

The Land at Neptune Wharf, Wyke Road, Bow, London E3 2PL

Neptune Group

29 November 2012

Prepared by

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DATE	*ORIGINATORS*	*APPROVED*
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29 November 2012
Our Ref: RLG/J028249

PRIVATE AND CONFIDENTIAL

London Legacy Development Corporation
Level 10
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For The Attention of Allison De Marco

Dear Madam

Economic Viability Analysis and Justification in Respect of:-
The Land at Neptune Wharf, Wyke Road, Bow, London E3 2PL

EXECUTIVE SUMMARY

On 1st November 2012 a planning application was submitted by the Neptune Group in respect of the redevelopment of the Land at Neptune Wharf, Wyke Road, Bow, London E3 2PL. The description of development as provided in the submitted planning application form is:

'Hybrid' planning application for comprehensive mixed use redevelopment of the site in up to 4 phases / zones containing up to 21 buildings to provide for a mix of land uses comprising:

1 Detailed element – Application for full planning permission for phases/zones 1 and 2 to provide 14 buildings including development comprising:

- Demolition of all existing buildings and removal of structures;
- Residential (Use Class C3) comprising 514 dwellings (45,447 sq.m GIA);
- Commercial floorspace within Use Classes A and B comprising 5,297 sq.m

GIA to include:

- Business premises (Use Class B1) including offices, light industrial workshops and studios 3,769 sq.m within Blocks A, C, G, H, I, J and K;
- local retail, service, and food and drink uses (within Use Classes A1, A2, A3, A4, A5) 1,528 sq.m within Blocks A, B, D, E, F, G and K;
- Provision of new site access points for pedestrians and vehicles with new internal access routes/streets and means of access and circulation; highway surface improvements and associated surface and underground parking for cars and cycles;
- Provision of new open spaces, including private amenity, communal amenity and public realm areas and associated landscaping works;

- Associated site works including excavation and re-grading of site levels including utility diversions, upgrades and new connections and other supporting infrastructure and engineering works.

2 Outline element – Application for outline planning permission (with all matters reserved except access) for Phases/zones 3 and 4 to provide up to 7 buildings including development comprising:

- Demolition of all existing buildings and removal of structures;
- Residential (Use Class C3) not exceeding but ranging between 11,451 sq.m and 24,298 sq.m, or between 142 and 293 dwellings;
- Flexible commercial/community floorspace within Use Classes A, B and D1 Use Classes comprising between but not exceeding 2,739 sq.m to 7,193 sq.m to include:
  - Local retail, service, and food and drink uses (within Use Classes A1, A2, A3, A4, A5) not exceeding but ranging between 660 sq.m and 1,126 sq.m
  - Business premises (Use Classes B1) including offices, light industrial workshops and studios not exceeding but ranging between 695sq.m and 1,613 sq.m.
  - 3 Form Entry Primary School (Use Class D1) not exceeding but ranging between 5,440 sq.m and 5,838sq.m with associated external play areas;
- Provision of new site access points for pedestrians and vehicles with new internal access routes/streets and means of access and circulation; highway surface improvements and associated surface and underground parking for cars and cycles;
- Provision of new open spaces, including private amenity, communal amenity and public realm areas and associated landscaping works;
- Associated site works including excavation and re-grading of site levels including utility diversions, upgrades and new connections and other supporting infrastructure and engineering works.

This report considers the financial viability of the proposals and provides justification in economic viability terms for the level of affordable housing and other planning benefits included within the planning application.

It is important to recognise that this project has evolved through detailed discussions with planning regulators and the Mayor's Office over the last 18 months. Key land uses and design approaches emerged from these discussions, including the provision of key public spaces, infrastructure and land use arrangements. It was only during August and September 2012, very late in the process that the request for a school site was put forward, along with the retention of previously agreed or desired planning and development moves. This has obviously presented challenges for all concerned, land owner, design team and regulator, and has led to the reformation and repositioning of the financial offer.

Based upon the findings herein the proposed scheme for the overall hybrid application shows a residual land value below what would be considered 'an appropriate Site Value for the landowner' in accordance with the RICS 1st Edition Guidance note GN94/2012 entitled 'Financial viability in planning' which was recently published. This is on the assumption of the following planning contributions:

- The provision of a 0.44 Ha (1.09 Acre) serviced site at a peppercorn for a new three form entry primary school. This equates to £2.18m in terms of an existing use land use value to the current landowner. More significantly however, in terms of lost profits to the developer this site contributed a far higher value and contribution to the overall scheme in a 'non-school' scenario, amounting to between £7m and £8.7m depending on the level of affordable provision.

- A contribution of £250,000 towards the cost of local infrastructure / accessibility improvements
- A contribution in kind towards Open Space/Landscaping/Playspace through the provision of three key spaces; Lofthouse Square, Smeed Gardens and Lockside Place having an area of circa 0.6 ha. (1.48acres) an existing use land value of £2.96m and at a landscaping cost of approximately £1.8m
- [redacted]The provision of a significant amount of commercial space within the scheme which is unlikely to be viable. The current cost estimate to the scheme based on the appraisal herewith is £[redacted]
- Community Infrastructure Levy of approximately £2,182,810
- Provision of zero on-site affordable housing on the assumption of nil Housing Grant
- A realistic market risk adjusted return to the developer - 20% on GDV

Notwithstanding the financial deficit and therefore risk at the outset of development, our client recognises the fact that certain minimum levels of planning benefit are required and they are prepared to proceed to deliver these.

Our client attended the recent Examination in Public in respect of the Fish Island AAP and made representations to the inspector at that time in respect of viability issues in connection with the potential need to deliver a school site. The inspector in his report attached herewith as Appendix VI makes it clear that Neptune Wharf is the right location for a school site and as such our client is prepared to make available a site for a new primary school. However the inspector also recognised the viability issues that the scheme faces and when talking about imposing the requirement for the school on the site he suggests in para 53 “However, this clearly means that other such requirements that might otherwise be sought or expected by the Council will have to be scaled back, or even omitted entirely, for viability reasons.” He also suggests that scheme density may need to be above the levels originally intended in order to allow the scheme to come forward.

Our client is prepared to assist in the delivery of the required north south links through a contribution to the delivery of a new bridge and is also prepared to deliver a serviced site for a new primary school at a peppercorn together with a significant amount of public open space. However there is a heavy financial burden and therefore the scheme does not include affordable housing and while providing considerable benefits in kind towards the section 106 is not able to provide any monetary benefits. The scheme therefore delivers the benefits sought by the local authority through scaling back other requirements which might otherwise be sought as suggested by the inspector.

1. INTRODUCTION

1.1 This report has been prepared on behalf of our Clients – Neptune Group – in order to consider the viability resulting from the proposed redevelopment of the site and demonstrate the level of affordable housing that it is viable to deliver within the proposed scheme on the assumption that grant funding will not be secured for the scheme and that it is necessary to provide a serviced primary school site at a peppercorn.

1.2 We have undertaken development appraisals using the industry recognised ARGUS Developer Model (formerly Circle Developer) and attach a summary as Appendix I.

1.3 The report will give a brief overview of the proposed scheme and detail the assumptions contained within the development appraisal. This will allow conclusions to be drawn in respect of the level of affordable housing and other planning benefits that it is economically viable to provide within the proposed development.

2. DETAILS OF THE PROPOSED DEVELOPMENT

2.1 We attach as Appendix II plans and accommodation schedule for the three phases of this scheme. Phases 1 and 2 of the scheme are submitted in detail and Phase 3 in Outline. Brief details of the proposed accommodation follow:-

Phase 1

Unit Type	Number of Units	Unit NSA (Sq. ft.)
1B 2P	84	551
2B 3P	9	691
2B 4P	113	771
3B 4P	14	863
3B 5P	19	1104
4B 7P	8	1457
	247	746
A1-A4 Uses		8547
B1 Uses		26285

Phase 2

Unit Type	Number of Units	Unit NSA (Sq. ft.)
1B 2P	79	570
2B 3P	0	0
2B 4P	139	783
3B 4P	20	868
3B 5P	25	1073
4B 7P	4	1389
	267	762
A1-A4 Uses		7588
B1 Uses		14607

Phase 3

Unit Type	Number of Units	Unit NSA (Sq. ft.)
1B 2P	60	571
2B 3P	7	700
2B 4P	61	766
3B 4P	14	845
3B 5P	0	0
4B 7P	0	0
	142	688
A1-A4 Uses		7104
B1 Uses		7481
Potential 3 Form Entry Junior School		62840

3. VIABILITY APPRAISAL

3.1 Attached as Appendix I are Argus Developer development appraisal summaries considering the proposed scheme.

3.2 Market Residential Values

3.2.1 Stratford has seen significant redevelopment in recent years, but not on a consistent and constant basis. Some schemes have been successful, others have failed completely; starts have stalled and funding has collapsed. The advent of the London Olympics generated huge interest in the area and the banking collapse put paid to a lot of that interest. The ongoing investment in Stratford from the Government and the Olympic drivers has managed to bring forward ambitious infrastructure and commercial schemes, which would not have come to fruition without them.

3.2.2 Although some of the schemes have been ambitious and daring in design, this has less impact on the resultant sales values than one might expect. Developments that have launched at unsustainable prices have stuttered, but those that have been realistic whilst still providing a good product have been very successful (Aurora by One Housing Group being one where the sales rates were excellent and the prices achieved were between £300 and £400 per square foot, comparing favorably to other schemes in the area).

3.2.3 What is apparent from talking to agents and looking at Land Registry records is the low level of transactions over the last twelve months, even with the approach and arrival of the Olympic Games. Clearly economic constraints have had a real effect and the reluctance of buyers to pay over the stamp duty threshold at £250,000 has impacted many schemes. The development at 142 Paul Street is a good example of how, regardless of unit size, buyers resist paying over the threshold, where all nine units have sold between £245,000 and £250,000 and vary in size from 730 to 930 sq ft.

3.2.4 The table of comparable evidence below gives an indication of the middle to lower end of the market in tough conditions. If one is more selective on the scheme and analyse all the sale prices against the sizes, there is a significant variation of £ per sq ft values. For example in the Lett Road scheme (The Edge) by Thornsett Group, the values achieved range from £380 psft to £502 psft on the most recent sales (Q4 2011 – Q1 2012). Indeed, some of the larger units did better than their smaller two bedroom counterparts, but as usual, the one bedroom units averaged the highest levels.

3.2.5 It is evident that buyers are increasingly choosy and new build apartments should offer both a good specification and comfortable living space. When pricing the subject scheme, the eventual per square foot sales levels are reduced by the larger unit sizes. What is increasingly evident is that the Stratford market is very competitive and whilst there is demand, the design and mix of the development is crucial to its success and eventual sale prices. The pipeline is significantly higher than most areas of London and there is a real danger of saturation, but the more developments that are completed, the better the area will become as a whole and now that the Olympics are over, the focus will on the holistic regeneration of the area combined with the legacy of the Olympic Park.

3.2.6 Car parking is provided in basement or undercroft car parks beneath the residential buildings. We have assumed the spaces would have a value of £[redacted] per space.

3.2.7

Address	Description	Sale Price	Agent
1 Bed Flats			
1 Q Building, 110 The Grove E15	Large one bedroom flat in a very contemporary scheme in the centre of Stratford	£220,000 June 2012/638 sq ft/£345 psqft	Land Registry/ Strettons
97 Gerry Raffles Square E15	One bedroom upper floor flat in popular centrally located block next to underground station and Westfield Shopping Centre	£172,500 September 2011/450 sq ft/£383 psqft	Land Registry/ Filtons
13 The Edge, 1 Lett Road E15	One bedroom third floor flat in recent scheme that sold well at its release.	£200,000 April 2012/535 sq ft/£373 psqft	Land Registry/ Bairstow Eves
21 Victoria Mills Studios, 10 Burford Road E15	One bedroom fourth floor flat in popular modern block situated to the south west of the town centre.	£210,000 Mar 2012/545 sq ft/£385 psqft	Land Registry/ Strettons

2 Bed Flats			
5/140-142 The Grove E15	Two bedroom first floor flat in recent development close to town centre.	£245,000 June 2012/689 sq ft/£355 psqft	Land Registry/ Bairstow Eves
136 Gerry Raffles Square E15	Two bedroom seventh floor flat in popular development in central Stratford.	£250,000 Aug 2011/710 sq ft/£352 psqft	Land Registry/ Hamptons
3 Hallings Wharf Studios, 1 Channelsea Road E15	Two bedroom ground floor flat in contemporary block to the south of the town centre.	£240,000 March 2012/740 sq ft/£324 psqft	Land Registry/ Victoria Knight
71 Hallings Wharf Studios, 1 Channelsea Road E15	Two bedroom fourth floor flat in contemporary block to the south of the town centre.	£249,500 March 2012/784 sq ft/£318 psqft	Land Registry/ WJ Meade
142 Paul Street E15	New development of nine two bedroom/two bathroom flats released earlier this year, eight sold and last one under offer.	£245,000 - £250,000 February-August 2012/730-930 sq ft/£270 - £340 psqft	Rockledge
3 Bed Flats			
36 Azura Court, 48 Wharton Road E15	Three bedroom upper floor flat in colourful recent scheme to the south west of the centre, received a mixed reception when originally released.	£330,000 May 2012/1168 sq ft/£282 psqft	Land Registry/ WJ Meade
118 Gerry Raffles Square E15	Fifth floor flat in central scheme, smaller than some other three bedroom units in the area, but popular with investors.	£290,000 July 2011/960 sq ft/£302 psqft	Land Registry/ Filtons

3.2.8 **Market Rents**

Local agents are very busy with rentals and have been for the whole of this year, hardly surprising with the Olympics and the low volume of sales transactions. Currently and ignoring any influence of the Olympics, rents are around £[redacted] per week (£[redacted] per calendar month) for one bedroom units, £[redacted] per week (£[redacted] per calendar month) for two bedroom units and £[redacted] per week (£[redacted])for three bedroom units. Although turnover is good, there are always a large number of units on the market to let, so landlords have to be pragmatic and take a good tenant when they can rather than wait to achieve a better level of rent.

3.2.9 Based upon our research it is apparent that existing schemes are selling in the second hand market at circa £350psf but new schemes are achieving in excess of this. Having regard to this and the fact that this is a large scheme with good quality open spaces, which will generate its own market, we have applied the following average values to the various unit sizes. Based upon the mix of units we calculate an average price across the scheme of £[redacted]psf. Details of this calculation are include in Appendix III.

Residential Unit Type	Estimated Sale price
One Bedroom (Two Person) av. 563 ft^2	[redacted]
Two Bedroom (Three Person) av. 695 ft^2	[redacted]
Two Bedroom (Four Person) a/v. 775 ft^2	[redacted]
Three Bedroom (Four Person) av. 860 ft^2	[redacted]
Three Bedroom (Five Person) av. 1,087 ft^2	[redacted]
Four Bed House (Seven Person) av. 1,434 ft^2	[redacted]

3.3 **Commercial Values**

3.3.1 The majority of residential schemes with ground and mezzanine floor accommodation both in the Stratford area have struggled to dispose of their commercial content. Examples include:

3.3.2 *One Stratford, High Street, E15* – 8,867 sq ft of ground floor commercial accommodation was constructed as part of a development of 301 apartments. Having been completed in 2009, at present 6,705 sq ft of accommodation remains available with only two of the six units sold. The most recent sale (unit 4 in March 2012) reflected a value of £129psf CV. Quoting prices are between £153-£175psf CV.

3.3.3 Icona Point, Warton Road, E15 – 16,564 sq ft of ground and mezzanine floor commercial accommodation was constructed as part of a development of 245 apartments. Having been completed in 2009, at present all of the accommodation remains available although two of the four units (5,896 sq ft) are currently under offer. Quoting prices for the accommodation is in the region of £200psf CV.

3.3.4 St Luke's Square, Canning Town, E16 – 44,907 sq ft of ground and mezzanine floor commercial accommodation was constructed as part of a development of 162 apartments. Having been completed in 2010, at present all of the accommodation remains available, with the letting agents reporting very little interest. Quoting rents for the accommodation are £15psf.

3.3.5 Rental values in the region of £[redacted]psf are realistic for the accommodation. As evidenced by the schemes listed above, the accommodation will take some time to let. We have therefore allowed [redacted] letting period and a [redacted] rent free period when capitalising the rental income.

3.3.6 With the exception of the larger unit in block B which might be suitable for a national restaurant operator of good covenant strength the accommodation will appeal to local neighbourhood retailers such as newsagents, bookmakers, launderettes, etc. As such, occupiers are likely to be predominantly independent retailers of lesser covenant strength. Based on the above we adopt a rent of £[redacted] and a yield of [redacted]% on these elements.

3.3.7 The properties will be constructed to a 'shell and core' finish but with a certain element of fit out including shop fronts as it is unlikely that the majority of tenants for these units will have capital resources to complete a full fit out. The same is true of the business space.

3.3.8 There is a reasonable level of demand for this size of office accommodation which is evidenced with the level of occupancy and values achieved at Waterfront Studios (Dock Road, E16) and Stratford Office Village (Romford Road, E15).

3.3.9 Whilst located in the Canning Town/Royal Docks area, Waterfront Studios (operated by GLE Properties) is a good example of the level of value that could be achieved at the accommodation on account of its position outside of a town centre. The centre comprises circa 48,200 sq ft of office accommodation and 66,200 sq ft of light industrial accommodation. At present the site manager reports that the light industrial accommodation is fully let at values between £8.50 and £10psf and the office accommodation 50% occupied with recent lettings being in the region of £15psf (actual rents achieved are in the region of £24psf which includes utilities estimated to be £9psf). Car parking at the centre is limited (circa 55 car parking spaces equating to 1 space per 2,080 sq ft of accommodation) and despite the centre being only 75% occupied, the car park is full, with values of £740p.a. per space being achieved. On street car parking is restricted by a single yellow line but this designation is largely ignored. The office suites are let in a fully decorated condition with carpets, but do not benefit from air conditioning.

3.3.10 Stratford Office Village (operated by Workspace) comprises 52,000 sq ft of office accommodation with Stratford Town Centre and currently 89% let. Quoting rents for accommodation of 500 sq ft or under is £20 psf with larger floors marketed at £17.50psf. Some recent transactions are listed below:

Unit 13 – 608 sq ft let at £18.95psf in March 2012 on a 10 month lease.
Unit 5 – 3,346 sq ft let at £17.25psf in January 2012 on a 12 month lease.
Unit 4 – 1,603 sq ft let at £16.00psf in November 2011 on a 5 year lease.

3.3.11 The above rents are all net rents, exclusive of service charge and business rates. Each property benefits from a car parking space; the accommodation has 60 car parking spaces equating to 1 space per 867 sq ft of accommodation. The office accommodation benefits from air conditioning.

3.3.12 Within Stratford Town Centre office, good quality office accommodation achieves rental values of between £17-17.50psf. Outside of the town centre, rental values are in the region of £12-13psf as illustrated by the following transactions:

Peter Heathfield House, 263 High Street – office accommodation of 1,685 sq ft located on the ground floor of a residential block. The accommodation was well presented having been recently decorated and benefiting from new carpets, air conditioning and two car parking spaces. The property let at a rent equating to £13.65 in March 2012.

Unit 4, One Stratford, High Street – a office unit located measuring 1,237 sq ft on the ground floor of a modern residential development sold for £160,000 in March 2012. The value achieved analyses to £129psf CV. The property was fully fitted out with new carpets, plastered and emulsion painted walls, air- conditioning and a W.C.

25 Moorey Close – a brick built detached building providing 5,478 sq ft of ground floor office accommodation. The accommodation benefitted from air conditioning, an attractive reception area and 14 car parking spaces. The property let at a rental value of £12.50psf in April 2011.

3.3.13 The level of on-site car parking and the specification of the properties will be significant factors as to the level of demand and rental value the new development will achieve. A good portion of occupiers will have staff who travel to work via car and as such parking provision (including on-street parking) will be an important factor for occupiers There is no parking identified for the commercial units. This is will deter potential occupiers.

3.3.14 As small commercial units, the premises will predominantly appeal to small and start up businesses. The majority of these have limited capital to undertake substantial fit out works and accommodation in which they can readily move into will be preferred. As evidenced by the rents achieved at Waterfront Studios, there is a substantial difference in values between light industrial and office uses (£8.50-£10psf for light industrial v £15psf for offices).

3.3.15 We consider the following rental values would be achievable:

Fit Out office accommodation with adequate car parking	£[redacted]psf
Fit Out office accommodation with little/no car parking	£[redacted]
Shell Units	£[redacted] psf

3.3.16 Based on the intended car parking provision and limited fit out allowed for in the build costs we have adopted a rental value of £[redacted]psf. We have allowed for a [redacted] letting period and rent free and capitalised the rent at a yield of [redacted]%.

3.4 Development Costs

3.4.1 We have been provided with construction budget costings prepared by our clients advisors – Gavin Johnson of Johnson Associates (UK) Ltd. We attach a full summary as Appendix IV.

3.4.2 Gavin Johnson will be pleased to discuss his cost plan further with the LLDC' advisor as required.

3.5 Development Phasing & Timescales

3.5.1 Our development appraisal assumes that the development comes forward as three residential phases. The detailed phasing can be seen within the appraisal summary attached as Appendix I.

3.5.2 Residential sales rates have been assumed at an average of 8 units per month across the scheme. Details of the sales periods are contained within the appraisal summary.

3.6 Planning Obligations

3.6.1 <u>Section 106</u>

In addition to the provision of a site for a new three form entry primary school at a peppercorn the scheme is making contributions in kind towards the local infrastructure / accessibility improvements, open space and the provision of a considerable amount of commercial business and retail units at a considerable cost. It is not currently financially viable to provide further cash payments towards section 106 items without affecting the elements already being offered.

3.6.2 <u>Benefits In Kind</u>

The scheme will deliver the following benefits in kind:

- The provision of a 0.44 Ha (1.09 Acre) serviced site at a peppercorn for a new three form entry primary school. This equates to £2.18m in terms of an existing use land use value to the current landowner. More significantly however, in terms of lost profits to the developer this site contributes a far higher value, the contribution to the overall scheme in a 'non-school' scenario, amounting to between £[redacted]m and [redacted]m depending on the level of affordable provision.
- A contribution of £250,000 towards the cost of local infrastructure / accessibility improvements
- A contribution in kind towards Open Space/Landscaping/Playspace through the provision of three key spaces; Lofthouse Square, Smeed Gardens and Lockside Place having an area of 0.6 ha. (1.48acres) an existing use land value of £2.96m and at a landscaping cost of approximately £1.8m
- The provision of a significant amount of commercial space within the scheme which is unlikely to be viable. The current cost estimate to the scheme based on the appraisal herewith is £[redacted]. This is shown in the appraisal included as Appendix V

The benefits in kind delivered by the scheme equate to a total sum of £[redacted] excluding any lost developers profit equating to £[redacted] per residential unit.

3.6.3 Community Infrastructure Levy (CIL)

We have assumed that CIL would not be charged on the school element as a nil charge rate is applied to it under the Mayor's current charging schedule. CIL on the remaining development can be calculated as follows:-

Assuming Nil Affordable Housing:

GIA of Total Development excluding School	71,749 sq. m
Less Existing Space in Occupation	9,383 sq. m
Area for Calculation of CIL	62,366 sq. m
@ £35 per sq. m	x £35
CIL Payable	**£2,182,810**

This equates to a further £3,327 per unit in planning benefits being delivered by the scheme giving a total of £17,252 per residential unit.

Any amendment to these figures would have an effect on the viability of the scheme as reported herein.

3.7 Marketing, Acquisition and Sales Fees

3.7.1 Details of the estimated marketing, acquisition and sales fees are contained within our appraisal (attached as Appendix I). The fees have been applied having regard to industry standards for a development of this nature.

3.8 Developers Return

3.8.1 RICS 1st Edition Guidance note GN94/2012 entitled 'Financial viability in planning' state the following in respect of the margin which should be adopted as a benchmark within viability appraisals:

'The benchmark return, which is reflected in a developer's profit allowance, should be at a level reflective of the market at the time of the assessment being undertaken. It will include the risks attached to the specific scheme. This will include both property-specific risk, i.e. the direct development risks within the scheme being considered, and also broader market risk issues, such as the strength of the economy and occupational demand, the level of rents and capital values, the level of interest rates and availability of finance. The level of profit required will vary from scheme to scheme, given different risk profiles as well as the stage in the economic cycle. For example, a small scheme constructed over a shorter timeframe may be considered relatively less risky and therefore attract a lower profit margin, given the exit position is more certain, than a large redevelopment spanning a number of years where the outturn is considerably more uncertain.'

3.8.2 This is a large project spread over a considerable number of years with considerable risks involved which will commence in financially uncertain times. Based on our knowledge of returns currently being sought by banks offering development funding and returns being required by developers we would suggest that the absolute minimum return that a scheme of this type will require to proceed is 20% of Gross Development Value. We include this level of return within our Gross Development Costs to arrive a residual land value to benchmark viability ie. being greater or less than what would be considered an acceptable site value.

3.9 **Appraisal Results**

3.9.1 We detail below the results of the attached development appraisal for the overall scheme (Appendix I):-

<u>Residual Land Value of the Scheme Assuming Nil Affordable Housing</u>

Gross Development Value	£[redacted]
Net Development Value	£[redacted]
Construction Costs	£121,750,000
Professional Fees	£13,510,000
Total Costs	£165,214,000
Residualised Land Value	**£**[redacted]
Residualised Land Value per Acre	**£**[redacted]
Profit	£[redacted]
Profit on GDV (%)	20%
Profit on Cost (%)	25.06%

4. **VIABILITY AND LAND VALUE**

4.1 We have undertaken a development appraisal of the proposed scheme based on the assumptions detailed above in order to arrive at a residual land value for the site.

4.2 The RICS recently published its 1st Edition Guidance note GN94/2012 entitled 'Financial viability in planning'. The purpose of the Guidance Note is to enable all participants in the planning process to have a more objective and transparent basis for understanding and evaluating financial viability in a planning context.

4.3 The Guidance Note defines financial viability for planning purposes as follows:

'An objective financial viability test of the ability of a development project to meet its costs including the cost of planning obligations, while ensuring an appropriate Site Value for the landowner and a market risk adjusted return to the developer in delivering that project'.

4.4 The viability appraisal summarised above and attached as Appendix I, takes into account the estimated values and costs of providing the proposed scheme and allows for a market risk adjusted return to the developer in order to compare the resultant residual land value with what would be an appropriate site value for the landowner.

4.5 In order to assess what is an 'appropriate site value for the landowner' we have considered a 'Red Book' valuation carried out for the landowner's bank which was based on the existing uses on the site. We have then allowed for a premium of 20% as a realistic landowner return over and above the existing use value. The valuation carried out by Lambert Smith Hampton states 'We are of the opinion that the current **Market Value** of the freehold interest of Neptune Wharf, Wyke Road, London, E3, as at 31 January 2012, in its current state, subject to the leases detailed herein, for loan security purposes, as described herein, is £9.15m. Adding 20% to this gives a figure of £10.98m equating to £1.926m per acre.

4.6 Our colleagues in GL Hearn's CPO team have recently undertaken an exercise to establish the cost of buying in the remaining lands required to bring forward a scheme at Chobham Farm on the other side of the Olympic village. They carried out in depth research into comparable land transactions that have taken place within the surrounding areas including the following:

4.6.1 **2-12 High Street, Stratford E15**

A site measuring 0.211 ha (0.52 ac) is currently being marketed by Savills and Blenheim Bishop at a guide price of £6,000,000. The site has planning permission for 191 apartments (579 habitable rooms) and 639 sq m (6,878 sq ft) of commercial accommodation over two buildings, one a 15 storey tower (44 units and commercial) and the other a 35 storey tower (147 units). The site density is very high, equating to 2,744 habitable units per hectare. The site is located at the western end of Stratford High Street, with a frontage opposite the elevated section of the Bow Interchange flyover. Whilst the scheme is 100% private, section 106 contributions of up to £7,728,000 (£40,460 per unit) are payable if a specified levels of gross development value is obtained.

4.6.2 The quoting price analyses to £10,363 per habitable room. We have discussed the progress of the disposal of the land with Mr Andrew Boyd of Savills who reported that they are currently in negotiations with a couple of parties to see if they can get a deal but the site is not currently under offer. On account of the number of high rise apartment developments along the High Street, modest sale rates, the high build costs associated with a tower development and the lack of opportunity to develop the site in phases meaning that a developer has a long lead in time before receiving income against development cost, there has been limited interest from parties wishing to acquire the site.

4.6.3 **Plaistow Hospital, Samson Street, E13 9EJ**

A site measuring 1.59 ha (3.93 ac) was sold for £6,750,000 in April 2012. The site was sold with planning permission for 97 apartments and 41 houses (437 habitable rooms) over a number of buildings ranging from two to five storeys in height. A number of the former hospital buildings will be retained and converted for residential use. The site density is low, equating to 275 habitable rooms per hectare. 32.5% of the units are affordable (60% social rent; 40% intermediate). Section 106 contributions totalled £567,120 equating to £4,110 per unit. The site is located a short distance north of the Barking Road, near to the junction of Green Street. The purchase price analyses to £15,446 per habitable room.

4.6.4 **Gun Wharf, Old Ford Road, E3 5QB**

A site measuring 0.484 ha (1.20 ac) was sold for £8,600,000 in November 2011. The site was sold with planning permission for 121 apartments (325 habitable rooms) and 110 sq m (1,184 sq ft) of commercial accommodation over four buildings, of between three and four storeys in height. 28% of the units are affordable (76% social rent; 24% intermediate). The site is a small industrial estate located in a residential area a short distance west of the A12. Immediately to the north of the site, on the other side of the Hertford Canal is Victoria Park. The purchase price analyses to £26,462 per habitable room.

4.6.5 **Sugar House Lane, Stratford, E15**

LandProp Holding BV purchased 8.387 ha (20.72 ac) of land at Sugar House Lane in two separate transactions for a total sum of £42,520,000 in October 2011. Planning permission has subsequently been obtained for a mixed use development of 1,200 units (3,662 habitable rooms), 58,133 sq m of commercial/community accommodation and a 350 bedroom hotel over a larger 10.5ha (25.95ac) site. The site density is modest, equating at 349 habitable rooms per hectare, although this density calculation doesn't reflect the large amount of commercial accommodation situated on the site; the majority of modern developments have commercial and residential elements within the same footprint whereas the Strand East development will have large parcels of land exclusively used for commercial uses. Consequently, the site density when analysed across the entire site is deceptive and cannot be readily contrast with other developments/planning permissions.

4.6.6 The purchase price equates to £5,069,751 per hectare (£2,051,700 per acre). When the site density permitted is applied to the land acquired by LandProp, the purchase price analyses to £14,536 per habitable room. To an extent, this purchase price reflects the need for some further land assembly.

4.6.7 In the height of the market, residential development sites along the High Street were achieving values well in excess of £20,000 per habitable room:

- Stratford One, 14-26 High Street: £23,418 per habitable room in April 2006
- Warton House, 150 High Street: £27,594 per habitable room in January 2008
- Aurora, 223-231 High Street: £23,313 per habitable room in June 2008

4.6.8 The CPO teams' conclusion, based upon a likely planning density of circa 600 hrh at Chobham Farm, was that a land value in the order £3m per acre is likely to be required to buy in the remaining lands required under CPO. In this case we adopted a land value of £2m per acre as being realistic for the lands already in the developer's ownership although arguably we could have adopted a higher figure.

4.6.9 The planning densities for the Chobham Farm site fall in the middle of the appropriate density range for Mid Fish Island set out in the Area Action Plan for Fish Island. We would therefore suggest that the appropriate site value should be similar if not a little higher. Indeed, reflecting the inspectors recent comments in his report on the Examination into the area action plan where he suggested that a higher number of units, at higher density and greater heights may have to be permitted to achieve a deliverable scheme, it could be argued that the value should be higher.

4.7 In addition to the sites mentioned in the CPO report we are fully aware of the background to the recent acquisition of the Chobham Manor site by Taylor Wimpey and L&Q as clients of GL Hearn, East Thames Group, also bid on the site. Although the bids were on the basis of a modest upfront deposit of £2m together with a percentage of revenues the winning bid suggested total income for the London Legacy Development Corporation is in the region of £80m for just under 23 acres or circa £3.5m per acre. Again this would suggest that adopting a figure of circa £2m per acre on the Fish Island site would be the minimum level of value the landowner would accept to release their land for development.

4.8 In assessing the ‘appropriate site value for the landowner’ for the site we have taken all of the above into account and adopted £2m per acre on the 5.7 acre site giving a total land value of £11,400,000.

4.9 Based on this range of comparable transactions, it is clear that the residual land value of approximately £[redacted] generated by the proposed scheme (with the level of planning obligations detailed above) does not provide the landowner with an appropriate site value in accordance with the RICS Guidance Note.

4.10 Notwithstanding the current financial position, our client recognises the fact that certain levels of planning benefit are required from a scheme of this kind and for this reason they are prepared to progress at these levels. Although our clients are prepared to work with the Planning Authority to ensure the scheme is a success, it is clear that the provision of further affordable housing or the requirement for any additional planning benefits would further impact on the viability of the project making it undeliverable in the current market.

5. CONCLUSIONS

5.1 The developer will be taking a risk at the outset of this scheme as they are reliant on the success of the scheme enhancing the current values pertaining for residential schemes in this area through the quality and size of scheme they intend to bring forward.

5.2 The viability of the site was questionable prior to the Tower Hamlets amending their Area Action Plan (AAP) – in a report on their behalf entitled Tower Hamlets Sites and Place Making Development Plan Document – Site Viability Testing, BNP Paribas concluded that at values of £403 psf, which are very similar to those adopted herein, the site could not viably provide a school of 0.4 ha and open space of 0.6ha. At the recent Examination in Public in respect of the Fish Island AAP the inspector accepted the viability concerns expressed by both ourselves and BNP Paribas. In his report attached herewith as Appendix VI, while he makes it clear that Neptune Wharf is the right location for a school site and as such our client is prepared to make available a site for a new primary school, he also recognised the viability issues that the scheme faces and when talking about imposing the requirement for the school on the site he suggests in para 53 “However, this clearly means that other such requirements that might otherwise be sought or expected by the Council will have to be scaled back, or even omitted entirely, for viability reasons.” He also suggests that scheme density made need to be above the levels originally intended in order to allow the scheme to come forward.

5.3 We have shown that based upon what is considered the minimum realistic market risk adjusted return to the developer which a scheme of this nature would require, of 20% on GDV, the scheme based upon current values produces a residual land value that would not be sufficient for a landowner to release the site for development. This is on the basis of the following planning contributions:

- The provision of a 0.44 Ha (1.09 Acre) serviced site at a peppercorn for a new three form entry primary school. This equates to £2.18m in terms of an existing use land use value to the current landowner. More significantly however, in terms of lost profits to the developer this site contributes a far higher value, the contribution to the overall scheme in a 'non-school' scenario, amounting to between £[redacted]m depending on the level of affordable provision.
- A contribution of £250,000 towards the cost of local infrastructure / accessibility improvements
- A contribution in kind towards Open Space/Landscaping/Playspace through the provision of three key spaces; Lofthouse Square, Smeed Gardens and Lockside Place having an area of 0.6 ha. (1.48acres) an existing use land value of £2.96m and at a landscaping cost of approximately £1.8m
- The provision of a significant amount of commercial space within the scheme which is unlikely to be viable. The current cost estimate to the scheme based on the appraisal herewith is £[redacted]
- Community Infrastructure Levy of approximately £2,182,810

5.4 Our client is prepared to assist in the delivery of the required local infrastructure / accessibility improvements through a financial contribution and is also prepared to deliver a serviced site for a new primary school at a peppercorn together with a significant amount of public open space. However there is a heavy financial burden and therefore the scheme does not include affordable housing and while providing considerable benefits in kind towards the section 106 is not able to provide any monetary benefits. The scheme therefore delivers the benefits sought by the local authority through scaling back other requirements which might otherwise be sought as suggested by the inspector.

5.5 Any requirement for further planning benefits would make the scheme undeliverable at the current time.

6. THIRD PARTIES AND PUBLICATIONS

6.1 Neither the whole nor any part of this report or any reference thereto may be included in any published document, circular or statement, nor published, reproduced or referred to any way without our prior written approval of the form and context in which it may appear.

6.2 This report is not a valuation for purchase, or sale, but an appraisal to give some indication of possible capital values. It does not constitute a formal valuation report and any indication of value may not be used for the purposes of obtaining finance, inclusion in balance sheets, sale or purchase of property. The projected estimates of value are based upon the information known to us at this time and do not constitute formal opinions of value.

Yours faithfully

GL Hearn

APPENDIX I

DEVELOPMENT APPRAISALS

APPENDIX II

PLANS AND ACCOMMODATION SCHEDULES

APPENDIX III

CALCULATION OF AVERAGE SALES VALUES

APPENDIX IV

BUILD COST

APPENDIX V

CALCULATION OF THE COST OF PROVISION OF THE COMMERCIAL SPACE

APPENDIX VI

INSPECTORS REPORT ON THE EXAMINATION IN PUBLIC OF THE FISH ISLAND AAP