CONFIDENTIAL

Affordable
Housing
Solutions

369-377 Kentish Town Rd
LB Camden

Financial Viability Report

February 2019
Affordable Housing Solutions Limited

Confidentiality statement

This report is strictly confidential to the Client.

It contains commercially sensitive information.

Accordingly, this report should not be disclosed (in whole or in part) to any person, or used for any purpose, unless consent to such disclosure or such use has been given by the Client.

Affordable Housing Solutions Ltd
7 Goldhawk Mews
London W12 8PA

tel: 020 8749 8178
abooth@ah-solutions.com
www.ah-solutions.com

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Affordable Housing Solutions Ltd
7 Goldhawk Mews
London W12 8PA

tel: 020 8749 8178
abooth@ah-solutions.com
www.ah-solutions.com

1.0 Introduction.

1.1 Affordable Housing Solutions, (AHS), have been appointed by KTR Carwash Project Ltd (the Applicant), to advise in relation to the affordable housing obligations that can be supported by the proposed redevelopment of the site of 369-377 Kentish Town Rd in LB Camden.

1.2 This explanatory report and the accompanying economic viability assessments, contain confidential and commercially sensitive information.

1.3 The proposals have been appraised employing an Argus appraisal. We understand that this form of financial model is acceptable to Camden Council for the purposes of determining the maximum viable quantum of affordable housing that can be supported with regard to proposed residential schemes, (as well as the maximum s106 contributions), and is, therefore, appropriate for purpose in relation to the subject project.

1.4 The purpose of the report is to provide an easily understandable and detailed review of the cost and revenue implications of the proposed development which drives the financial viability model. Our intention is to offer full transparency as regards the ability of the project to subsidise affordable housing generally.

1.5 On a project specific basis, the financial viability model, (attached as *Appendix 1*), demonstrates that the scheme cannot support any affordable housing obligations whilst still remaining viable.

2.0 The Proposed Development

2.1 The scheme provides commercial at basement and ground floor levels, with 14 flats above on first to sixth floors.

2.2 The site is adjacent to the railway line so the development will require licences and works carried out to the satisfaction of Network Rail.

2.3 The site is currently under-used as a car wash, with an advertising hoarding.

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2.4 The proposed housing mix is as follows:

Unit Type	Number	Average Size sm
1 beds	4	50
2 beds	8	72.97
2 beds split level	2	90.48

2.5 The planning consent must of course deliver a financially viable project in order to provide a suitable foundation for subsequent project delivery. For sites that do not provide the policy compliant affordable housing then a financial viability will be sought.

2.6 A sliding scale applies in Camden for sites with the facility to provide between 10 and 25 units. (Policy H4). For this scheme the target would be 28% as affordable housing. The affordable housing provision in line with the policy target would be 4 units on-site.

2.7 Regarding abnormals associated with the scheme, the planning statement has highlighted the following:

- Restrictive covenants held by Network Rail require that significant financial contribution is made where development is forthcoming on land immediately adjacent to their interests and infrastructure to release these covenants. These costs would not arise on most development sites and will be payable regardless of the final scheme that is approved.
- In physical terms, developing next to a live railway means that what can be built and where is restricted. Below ground level no piling is allowed within 3 metres of the retaining wall to the railway embankment which significantly reduces the development capacity here
- To allow upper floors to be maximised despite the limitations on areas, noted above, a structural solution of cantilevering over the ground level has been adopted
- At ground level an access of a minimum of 1m width must be maintained along the full length of the railway wall to maintain aces for Network Rail in this area. Again, this reduces the development

area available at ground floor and, thus, reduces the total floorspace that can be achieved on-site. The building is also set back 1.5m from Kentish Town Road frontage to enable pavement widening.

3.0 Method of Financial Viability Assessment

3.1 This explanatory report and the accompanying economic viability assessments, all contain confidential and commercially sensitive information.

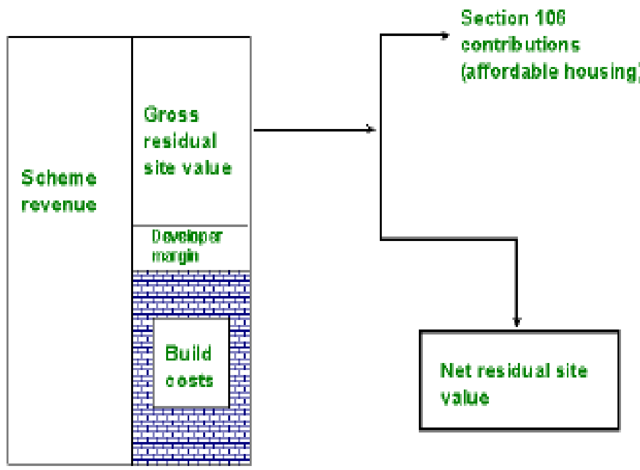
3.2 The Argus Development Appraisal software has been employed to define the financial parameters of scheme. We understand that this model is acceptable to the Borough for the purposes of determining the viable quantum of affordable housing that can be supported with regard to the scheme, and is therefore, appropriate for purpose in relation to the subject project. The Argus Appraisal for the proposed scheme is attached as *Appendix 1*.

3.3 The financial viability model is founded on the calculation of a net residual land value for the proposed development. Residual valuation is a frequently used method for appraising the financial viability of development schemes, whether new developments, or refurbishment of existing buildings.

3.4 The residual land value (RV) is then compared with a benchmark against which the viability of the scheme can be appraised. In this regard, the comparator should normally be the Existing Use Value of the site plus a suitable land owner's premium (EUV Plus); suitable Alternative Use Values, (AUV), and the Site Value (SV; RICS Viability in Planning). The net residual valuation can be expressed as a simple table:

Affordable Housing Solutions Ltd
7 Goldhawk Mews
London W12 8PA

tel: 020 8749 8178
abooth@ah-solutions.com
www.ah-solutions.com



3.5 The submitted viability assessment identifies the returns for developers and landowner generated by the scheme, and provides information to consider whether such returns are competitive in comparison to alternative options, which might include:

- Retention of the site;
- Sale of the sites for on-going existing uses
- Alternative development proposals.

3.6 The Mayor's Affordable Housing and Viability SPG, (2017), at 4.1.6 it recognises that AUV is a legitimate benchmark for financial viability modelling purposes. An AUV benchmark "*must also reflect policy requirements*". In addition the alternative use must "*fully comply with development plan policies and it can be demonstrated that the alternative use could be implemented on the site in question".*

3.7 As well as the preferred EUV Plus, and the AUV, in certain circumstances it accepts that it may be appropriate to use a land value based on an agreed market value, as set out by the RICS Viability In Planning guidelines, if applied correctly

3.8 The Harman Report refers to the concept of "*Threshold Land Value*". Harman states that the '*Threshold Land Value should represent the value at which a typical willing landowner is likely to release land for development*.' (page 28).

3.9 At numerous points throughout the report, Harman advocates, that the outcome of this approach will need to be “sense checked” against local market evidence. (Pages 29, 30, 31, 34, 36, 40)

3.10 Indeed the report does acknowledge that, ‘*if resulting Threshold Land Values do not take account* [of local market knowledge]*, it should be recognised that there is an increasing risk that land will not be released and the assumptions upon which a plan is based may not be found sound.*’ (page 30).

3.11 The EUV for this site is based on a less than optimum site coverage. The existing uses are confined to a car wash and an advertising hoarding and take up only c60% of the site. It is reasonable to expect that any land owner would want a significant uplift on the poor current use of the site as an incentive to sell.

3.12 In terms of providing an AUV, the site is allocated for development within the Kentish Town Neighbourhood Plan.

The Neighbourhood Plan is a formally adopted part of the Development Plan in Camden. As such, it has the same status as Camden’s own Local Plan and as such considerable weight must be attached to its content.

With reference to the car wash site, the Neighbourhood Plan allocation is clear that this site should be brought forward for development that provides a mix of retail use at street level with residential units on the upper floors.

The existence of this allocation is a positive and strong indication of support for the principle of development of this site. However, the specific allocation means that a mixed retail and residential development is the only form of development that could realistically come forward. Any other proposal for the site (for example, an office development) would be contrary to the Development Plan and thus should not be supported if a planning application was proposed.

Therefore, considerable weight must be given to the development potential of the site in accordance with the Neighbourhood Plan allocation. However, only limited weight can be given to the potential for alternative developments since this would not be in accordance with the Development Plan.

The only use that could be permitted on site, other than residential, would be retail at ground floor.

3.13 In order to take account of local market knowledge (see 3.9 and 3.10 above) we have also looked at the market value approach. We have referred to the RICS Viability in Planning Guidelines and adjusted any local site sales to take account of the comparable reflecting full compliance with development policy.

4.0 Proposed Scheme: Revenue Data

4.1 <u>Private Residential Values</u>

The values put forward by Goldschmidt & Howland are £9.25m or c£890psf. Their pricing schedule is set out as *Appendix 2.*

Another local agent, Salter Rex, estimated the values to be nearer £9.175m or £883psf. A third agent (Savills) valued them even lower.

For the purposes of this appraisal we have used the higher figure of £9.25m.

4.2 <u>Residential Ground Rents</u>

We have assumed ground rents of £300pa for 1 bed and £350pa for 2 bed. This has been capitalised at 5%. It should be noted that discussions are ongoing and legislation may be introduced in respect of ground rents and so there is a risk that this revenue will not be forthcoming and due to this risk 10% has been applied in other similar instances and we reserve the right to apply that in this instance.

4.3 <u>Commercial</u>

The local agent, Goldschmidt & Howland, have estimated these to be £40psf for ground floor and £24.60psf for basement with a yield of 5.5%. We have assumed a 6 month rent free period for fit out.

5.0 Proposed Scheme: Cost Data

5.1 <u>Proposed Scheme Construction Costs</u>

The current day construction costs for the proposed scheme have been assessed at £5.39m by Bristow Johnson. The Cost Plan for the Proposed Scheme is attached as *Appendix 3.*

We have not taken into account the inflation from today's date estimated by the QS, but included within their build cost plan, for the purposes of this appraisal.

There are several abnormal build costs applying to the proposed scheme. The main abnormal costs included within the build cost are:

- Network Rail (NR) requires a 1m maintenance zone along the boundary wall. NR will not permit any piling within 3m proximity to the boundary wall, which requires any building in that area to be cantilevered – c£300k. This is the QS estimate of the additional structure required. As this is a tight site and the planning requirements are for a fully stepped building at the front then using the full potential of the site is obtained by a cantilevered structure.
- Additional preliminaries for location and logistical issues (construction traffic, local traffic, pedestrians etc) – c£350k. The QS confirms that the construction period will be longer because of the restrictions on construction traffic and their ability to access the site, the location at a junction and the maintenance of pedestrian routes around the perimeter. There will need to be cantilevered temporary construction over the pedestrian footpaths. Logistically this is a tight site to construct.
- Enhanced brickwork and glazing to façade for this gateway scheme – c£430k. This includes for higher specification brickwork, Flemish bond brick format, stone cladding etc.This is to meet the requirements of planning for the appearance of the scheme and the estimate is only for the enhanced cost over and above the cost of a more traditional façade. The prominent nature and triangular shape of the site means that the building will have two primary elevations that together entail the majority of the building façade. Uniquely, given the triangular nature both these elevations require significant architectural treatment.

Additional abnormal costs that are not included within the build cost plan or the appraisal but which may be incurred:

- Triple glazing rather than double glazing as site between busy railway and road – c£80k. This has not been confirmed but it is an additional cost which might have to be spent.

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- Anti-vibration measures in structure – not known at this stage but may be required due to the proximity of the railway.
- Additional costs associated with the basement – the full costs of this are not known as yet.
- The building is set back 1.5m from Kentish Town Rd to accommodate an increase in pavement width.

5.2 Professional Fees

We have allowed for 12%.

There will be additional costs to the scheme to cover non-standard payments and fees, for example party wall, which have not been included at this stage. Additional details can be provided to the assessor. Nor have we included for the monitoring costs for Network Rail as these have not yet been estimated but they could be in excess of £100k, based on advice from the QS. As a result 12% for professional fees has been included.

We have allowed for a further £465k to cover release of restrictive covenants from Network Rail and associated insurance and legal fees. These have been agreed with Network Rail and relate to redevelopment of the site, as it is adjacent to the railway lines.

5.3 Contingency

A modest contingency of 5% has been applied. However, given the possible additional build costs and fees which may be incurred, we reserve the right to increase the level of contingency for the scheme.

5.4 Interest

A competitive debt interest rate at 6.75% has been employed within the viability assessment model. For current purposes we have assumed that this includes arrangement, bank monitoring, and exit fees.

5.5 S106 Contributions and CIL

The financial appraisal makes provision for the payment of Borough and Mayoral CIL of £750,000. This is an estimate provided by the planning consultant to include index linking.

Zero Carbon Tax at £2,300 per unit has been included.

5.6 Developer's profit

We have applied a profit of 18.5% of GDV for the market sale residential and 15% for the commercial. Given the current market conditions and the risks involved with residential development and the particular risks associated with this site, we believe the profit for the residential should be at least 18.5%.

5.7 Acquisition costs

These have been included at industry standard rates.

5.8 Marketing, disposal and letting fees

Marketing and disposal costs for residential have been inputted at 2.5% and 1.5% for commercial, with 0.5% for legal fees.

Letting fees for commercial have been inputted at 10% and legal at 5%.

6.0 Benchmark Land Value: Revenue Data

6.1 The Mayor's Affordable Housing and Viability SPG 2017 states that the EUV Plus route is preferred but that alternative approaches, such as AUV and market value, will be considered in exceptional circumstances, particularly if the latter is applied correctly and properly adjusted. The site benchmark should incentivise release of a site for development and ensure that the landowner receives a 'competitive return'.

6.2 The site is currently underused as a car wash and office, with additional revenue from an advertising hoarding. Colliers have valued this at £480k (see *Appendix 4*)

6.3 With a change in arrangements to the interior of one of the buildings, by inclusion of an additional floor in the 2.5 storey void, value could be added to the existing use, without affecting the external or extending into the site area. Colliers have given this a net additional value of c£65k, giving a total EUV of £545k. The buildings would still only offer a c60% site coverage and so will still be an underuse of the site.

6.4 It should be noted that the demand for a car wash, office and advertising hoardings, although not the optimum use of the site (taking up only c60% of site coverage), is high and this income would be easily secured

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in the future. This alone would suggest a premium at the top end of the range.

6.5 In terms of EUV Plus, we believe the premium should be at a maximum level and, even then, given the particular characteristics of the site the usual premium level may not equate to a threshold land value which would incentivise the land owner to sell the site for redevelopment. There is a high demand for these current uses in this location, but the site is also underused (at c60%), although it is situated in an important and prominent location. There is a site allocation attached to 369-377 Kentish Town Rd for development for retail and residential use. The GLA guidelines state "*the return the landowner requires will vary according to a range of factors including…. long term investment potential of the site.*"

6.6 As no use other than residential can meet planning requirements (and so no AUV is available), and taking into account the necessity of testing against local market knowledge, as set out in the Harman Report (clauses 3.8, 3.9 and 3.10 above), a site value, using the comparison method of valuation, has been undertaken. The site value methodology complies with the RICS Viability in Planning definition.

6.7 To this end we have asked Colliers to also look at the market value of the site, specifically with regard to the RICS Financial Viability in Planning guidelines. Colliers have looked at a number of site sales in the area, adjusted these to take account of commercial uses and where the sites have not been developed to provide the full affordable compliant policy, they have been adjusted to assume so. They have then deducted £465k for release of the restrictive covenants by Network Rail (which relate to the redevelopment of the site). Their report is attached as *Appendix 4.*

6.8 Colliers' view is that, based upon these RICS guidelines, and taking into account the release of restrictive covenants, the site benchmark under a market value approach would be in the order of £1.1m for planned residential use and c£1.35m including commercial. This value is based upon the number of units and habitable rooms for the proposed scheme, rather than for the site area, and so takes account of the site restrictions.

6.9 The values for the site benchmark in the scenarios above are as follows:

Existing use	£480k
Extending current use within the buildings	£545k
EUV Plus at say 50% premium	£818k
Market Value (residential use only)	£1,100k
Market value (both uses)	£1,350k

In conclusion, we believe that the appropriate site benchmark, to incentivise the land owner to sell the site for redevelopment, should be £1.35m. The current use applies to a very under-utilised site but in a very important location and the market testing supports this level of site benchmark for this particular site.

8.0 Appraisal Outputs

8.1 The financial appraisal of the Proposed Scheme, without affordable housing, results in a current residual land value of £695k (*Appendix 1*).

8.2 The site benchmark is £1.35m.

8.3 The proposed scheme cannot, therefore, support any affordable housing.

9.0 Conclusion

9.1 The Proposed Scheme has been appraised employing recognised residual valuation methodology expressed through the industry standard Argus model. We understand that this approach is acceptable to the Council for the purposes of determining the maximum viable quantum of affordable housing in mixed use projects containing residential use and is therefore, appropriate for the purpose in relation to the Proposed Scheme.

9.2 The Applicant has employed independent, suitably experienced and professional consultants to robustly analyse the cost and value implications of the Proposed Scheme and thus deliver robust data to populate the economic viability assessments.

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9.3 The site has a set of unique circumstances which mean that it cannot support affordable housing on-site, off-site or any financial contribution. These unique circumstances include:

- Restrictive covenants for any redevelopment
- Build costs associated with the structural solution resulting from adjoining Network Rail land and live railway lines
- Build costs associated with the site location on a busy junction
- Restrictions to the usable site, and thus the development footprint, resulting from the requirement to extend the footpath by the Council and requirements of Network Rail due to adjoining their land
- Costs associated with Network rail monitoring and other additional fees and costs associated with the development
- To provide a design of exceptional appearance to meet the expectations of the Neighbourhood Plan that will require a high level of material and finish and thus cost. The triangular shape of the site requires two primary elevations of high architectural quality

9.4 As a result it is unable to provide any of the 14 units as affordable to stay viable, or support off-site affordable housing or a Payment-In-Lieu. However, it does provide a considerable sum of CIL for Camden Council and allows for the redevelopment of an important strategic site in the Borough from its current unattractive and sub-optimum use.

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