No 7abc Bayham Street, NW1 0EY

Independent Viability Review

Prepared on behalf of the London Borough of Camden

2nd November 2018

Planning reference: 2018/3647/P

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1.0 INTRODUCTION

1.1 We have been instructed by Camden Borough Council to undertake a review of viability in respect of the current planning application to redevelop land at 7abc Bayham Street.

1.2 The proposed scheme will entail the demolition of the existing buildings on site and delivery of a 3-5 storey building (with two basement levels) comprised of office (B1a) and hotel (C1) uses, together with ancillary café/bar and gym facilities. The hotel will include 61 rooms and will be located across the basement to 4th floors. The B1 space will be on the basement, lower ground and ground floor.

1.3 Much of the basement will be used as conference rooms, a gym and changing rooms. Most of the lower ground is office space, including open plan areas and cubicles. The ground is split between the hotel lounge, the bar/café, and the co-working space, and these are not physically separated, so there will be interchange between these uses. The upper floors are all hotel rooms.

1.4 The application site of is bounded by three terraced houses (3,5, and 7 Bayham Street) to the south, a privately-owned car park (12 Camden High Street) and Mews houses (1a and 2 Kings Terrace) to the west, and two terraced houses (9A & 9B Bayham Street) to the north. The buildings on-site consist of two 2-storey commercial buildings, and one single storey pitched roof office, and the remainder of the site is a car park.

1.5 The applicant, Camden Lifestyle (UK) Ltd, instructed GL Hearn to prepare a viability assessment. This 17th August assessment concludes that scheme cannot afford to accommodate any affordable housing on-site. This appraisal includes £254,484 of CIL contributions, which is the only planning contribution shown in the appraisal.

1.6 The Council advised the applicant, during pre-application process, that in the absence of on-site residential provision a housing/affordable housing contribution (payment in lieu) would be sought with any subsequent planning application. The total payment-in-lieu was calculated by the Council at £1,998,792.

1.7 We have had regard to policy DP1, which requires any commercial development providing over 200 sqm of space, to provide 50% of that space as residential accommodation, subject to viability testing. This would, we understand, result in a requirement some of the proposed scheme's additional floorspace be delivered as housing. Policy DP1 generally requires this housing to be delivered on-site, especially in respect of schemes where the uplift in floorspace is over 1,000 sqm. However, the policy also states that, "*Where inclusion of a secondary use is appropriate for the area and cannot practically be achieved on the site, the Council may accept a contribution to the mix of uses elsewhere in the area, or exceptionally a payment-in-lieu.*" DP1 explains how the requirement for off-site housing should be calculated:

"For example, an additional 800 sqm of non-residential development without on-site secondary uses could either be matched off-site by the addition of 800 sq m of housing floorspace (with no reduction of existing non-residential floorspace), or matched by the conversion or redevelopment of 400 sq m of non-residential space into 400 sq m of housing."

1.8 Our Viability Review has scrutinised the cost and value assumptions that have been adopted in the viability assessment, in order to determine whether the current affordable housing offer is the maximum that can reasonably be delivered.

1.9 The advice set out in this report is provided in the context of negotiating planning obligations and therefore in accordance with PS1 of the RICS Valuation - Professional Standards (January 2014) (Red Book), the provisions of VPS1 – 4 are not of mandatory application and accordingly this report should not be relied upon as a Red Book Valuation.

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

2.0 CONCLUSIONS & RECOMMENDATIONS

Viability results

2.1 GL Hearn have undertaken a development appraisal of the application scheme. The applicant is not proposing to deliver any housing within the scheme, and no housing/affordable housing contributions are being offered; on this basis, the appraisal generates a residual land value of -£391,773 (and this appraisal assumes total CIL payments of £254,484). This is considerably below the estimated benchmark land value of £5.31m. It indicates that the scheme cannot viably make any additional planning contributions, and we question why the applicant is willing to proceed with the scheme given this apparent level of deficit.

2.2 Our review of the cost and value assumption in the appraisal indicates that most of the appraisal inputs are realistic and supported by market evidence. We have suggested changes to the compensation costs, the yield applied to the existing offices, and the rent applied to the new offices – and all these changes act to improve viability, but are insufficient to overcome the substantial viability deficit. We therefore agree with the conclusion that the scheme cannot realistically deliver any form of housing/affordable housing contribution, based on present-day costs and values.

2.3 One of the key reasons for the struggling viability of the scheme is the substantial build costs, due to this being a complex mixed use scheme within a small, constrained site, in an area of London that has typically high build costs. Residual valuations are highly sensitive to changes in costs and values over time, therefore we recommend that the Council considers seeking agreement to a deferred contributions mechanism, based on outturn costs and values, so that if improvements in viability result in a profit surplus being generated, this can trigger cash payments in respect of housing/affordable housing.

2.4 We discuss in the remainder of this conclusions Section, our key conclusion regarding the main inputs into GL Hearn’s development appraisal.

Benchmark land value

2.5 The existing use valuation (EUV) estimated by GL Hearn is £3,385,000. A landowner premium of 30% is allowed for. The premium is £1.2m and is calculated as a percentage of the figure of £4.085m which is the EUV plus the compensation costs. We question whether a premium is required over the compensation costs, as this compensation is by definition an incentive for the tenant to vacate thus an addition premium is not required. We have opted to base the premium directly on the EUV, and reduce it to 20% which reflects the moderate quality of the existing uses on-site. This gives a total benchmark of £4.76m (inclusive of the £700,000 of compensation costs) assuming both the EUV and compensation costs are reasonable.

2.6 We have assessed GL Hearn’s existing use value, which properly takes into account the existing tenancies on-site. The yield adopted is 5.75% (although with a higher yield of 6.5% which relates to the portion of income that exceeds the Market Rent for over-rented properties). This compares to the yield of 5.5% applied to the proposed scheme's office space, thus it appears there is insufficient differential between the proposed scheme's offices and the existing offices. We discuss office yields further in Section 6, below. We have suggested a yield of 6.5% for the existing offices, which makes allowance for their condition and factors in to this yield potential refurbishment costs. This would reduce the benchmark by circa £400,000, although we are unable to calculate this precisely without access to an electronic version of the existing use valuation.

Compensation costs

2.7 With respect to the compensation costs, there are three years remaining on the existing leases, and £650,000 has been allowed for buying out these tenants. This is the Market Rent of the leases. It is not clear why the full market rent would need to be paid. This appears to be an excessive level of compensation. It would be typical in our experience for the compensation to amount to the relocation costs incurred by these tenants together with some additional incentive. This point therefore requires further discussion.

Development costs

2.8 With respect to the build costs, our Cost Consultant Neil Powling has concluded that these are reasonable, based on his comparison with BCIS average tender prices. In addition, we are in agreement with all the other cost inputs in the appraisal, including among others the professional fees and finance costs.

Value of proposed offices

2.9 Looking at other lettings nearby lettings, we have analysed these in **appendix two**. These lettings indicate that £45 per sq ft is potentially understated for new-build offices in this location, as circa £55.00 has been achieved for second-hand 'media-style' (i.e. not grade A) offices locally. Whilst Bayham Street is not an 'established' office located, as GL Hearn note, this is unlikely to be a significant issue given the close proximity to the centre of Camden Town and the tube station. Based on this, we have adopted £55 per sq ft for the ground floor. We have maintained the 70% and 50% discounts for the lower ground and basement respectively, and the overall increase in GDV is £392,000. There is, however, an interplay between rents and yields, and the more the optimistic the adopted rents are, the more pressure there is on yield due to increased risk attached to the rental income.

Affordable workspace

2.10 The Council's policy requires 20% of the office space to be at 50% of Market Rent. This has been achieved by reducing the overall rent of the offices by 10%. Given the relatively low level of the Market Rents on the lower floors, it should be established by the Council whether this policy applies in this case. In addition, given that the end-users of the space will not directly benefit from this rent reduction (as they will be licensees) it is unclear how useful it will be for this type of serviced office/hub arrangement.

Value of proposed hotel

2.11 Regarding the valuation of the hotel, we are in agreement with the assumptions used, including the yield, room rates and operating costs. These have all been fully supported and evidenced by a very detailed report by hotel specialist White Bridge.

3.0 BUILD COSTS

3.1 With respect to the build costs, our Cost Consultant Neil Powling has concluded that these are reasonable, based on his comparison with BCIS average tender prices. He concluded: *"Our benchmarking yields an adjusted benchmark rate of £4,054/m² that compares to the Applicant's estimate of £4,146/m² a difference of £92/m² (£279,700). Despite this difference in benchmarking and based on consideration of the detail in the cost estimate, we consider the costs to be reasonable"*. His full report is in **appendix one**.

3.2 The construction period is 24 months for the office and for the hotel. There is a 6 month pre-construction period for each. And for the office these is a letting period of 6 months and a sale period of 6 months. These are realistic assumptions. The finance costs are calculated based on a reasonable interest rate of 6.5%.

3.3 There is a 10% allowance for professional fees, and 5% for contingency, which are both in line with typical benchmark rates. However, in view of the complexity of this mix use scheme a higher level of professional could potentially be justified. Other cost inputs, including the sales agent and legal fees, are in line with typical rates.

3.4 The profit adopted is 15% on GDV across the whole scheme. It totals £2.82m. This compares to the Planning Practice Guidance (July 2018 update) which that "15-20% of gross development value (GDV) may be considered a suitable return to developers in order to establish the viability of plan policies". There is considerable risk involved in this scheme given the uncertainty over which hotel operator will be secured and what the precise arrangement will be with this operator. A profit of 15% on GDV is typical for development of commercial space thus this can be considered reasonable.

4.0 COMPENSATION COSTS

4.1 There are three years remaining on the existing leases, and £650,000 has been allowed for buying out these tenants. This is the Market Rent of the leases. It is not clear why the full market rent would need to be paid. This appears to be an excessive level of compensation. It would be typical in our experience for the compensation to amount to the relocation costs incurred by these tenants together with some addition incentive. This point therefore requires further discussion.

4.2 7c Bayham Street is inside the Landlord & Act 1954 “Security of Tenure” provisions. The rateable value is £51,000, and the compensation is limited to this figure as per the Act.

5.0 EXISTING USE VALUATION

5.1 The existing use valuation (EUV) estimated by GL Hearn is £3,385,000. The White Bridge report states that, *"The site lends itself well to redevelopment as the existing office premises and courtyard are highly inefficient and of low quality",* although White Bridge are not directly involved in valuing the existing offices. We have therefore requested further comments from GL Hearn regarding the condition of the offices, and they have provided a description of each unit which confirms that they are in reasonably good condition and provide a moderate level of specification.

5.2 The application site is bounded by three terraced houses (3, 5, and 7 Bayham Street) to the south, a privately-owned car park (12 Camden High Street) and Mews houses (1a and 2 Kings Terrace) to the west, and two terraced houses (9A & 9B Bayham Street) to the north. The buildings on-site consist of two 2-storey commercial buildings, and one single storey pitched roof office, and the remainder of the site is a car park.

5.3 The excellent location and the large demand in Camden for media-style offices means there is a strong potential for lettings in this location even for 'secondary' offices that are not in top condition.

5.4 The rents applied in the existing use valuation are the passing rents, up to the reversion (i.e. rent review) dates for each of these, at which time these revert to market rents – which are in any case not increased from the passing rent levels. Given that these are passing rents, we accept that they are suitable to adopt for valuation purposes. The rents are consistent with similar-standard offices such as some of those detailed in **appendix two**, which details recently office lettings.

5.5 The yield adopted is 5.75% (although with a higher yield of 6.5% which relates to the portion of income that exceeds the Market Rent for over-rented properties). The yield applied to the new-build space is 5.5% (gross) thus it appears there is insufficient differential between the proposed scheme's offices and the existing offices. We discuss office yields further in Section 6, below; and comparable lettings evidence is provided in **appendix three**. We have suggested a yield of 6.5% for the existing offices, which makes allowance for their condition and factors in to this yield potential refurbishment costs. This would reduce the benchmark by circa £400,000, although we are unable to calculate this precisely without access to an electronic version of the existing use valuation.

6.0 PROPOSED OFFICES – VALUES

Office Rents

6.1 The offices will be targeted at SME's, start-up companies and freelance workers, and the applicant will seeking lettings to providers such as WeWork, Club Workspace and Impact Hub.

6.2 The rent tone for new-build space is cited as £45 per sq ft. The new-build offices are assumed by GL Hearn to be fit out to Cat A standard by the developer: "*We have assumed that the developer will build and fit out the office to a Cat A standard ready for a tenant to lease the premises and complete their own tenants fit out. In light of this we therefore adopted a higher baseline rent compared to the existing office space (itself in good condition,….).*"

6.3 We have taken into account that the space is on basement-ground floor, thus is overall less attractive than comparable upper floor offices. One example given to demonstrate the level of discount attributable to lower ground floors is 17-21 Wentlock Road where the ground floor let for £49 per sq ft and the lower ground let for £35 per sq ft – thus 29% lower. We accept that this is a realistic level of reduction for lower ground space. This is the level of reduction GL Hearn have applied to the £45 per sq ft 'tone' (applied to the ground floor) to reach their £31.50 per sq ft rent for the lower ground. For the basement below this, a greater discount of 50% is applied to reach £22.50 per sq ft.

6.4 The comparable evidence nearby includes lettings at the subject site itself, for example the April 2018 rent review of Unit 7a Bayham Street at £35 per sq ft. It is realistic to add a premium to this to reach the rent of a new-build office. And Unit 7b's rent was reviewed up to £40 per sq ft in December 2017. It appears that a £5 per sq ft increase is insufficient to account for the difference in quality between the existing space and the proposed (ground floor) offices.

6.5 Looking at other lettings nearby, we have analysed these in **appendix two**. These lettings indicate that £45 per sq ft is potentially understated for new-build offices in this location, as circa £55.00 has been achieved for second-hand 'media-style' (i.e. not grade A) offices locally. Whilst Bayham Street is not an 'established' office location, as GL Hearn note, this is unlikely to be a significant issue given the close proximity to the centre of Camden Town and the tube station. Based on this, we have adopted £55 per sq ft for the ground floor. We have maintained the 70% and 50% discounts for the lower ground and basement respectively, and the overall increase in GDV is £352,000 (which takes into account the affordable workspace).

Office Yield

6.6 The yield adopted to capitalise the estimated rent, is 5.5%. We have had regard to the Knight Frank yield guide which shows a 4.25% yield for City Prime, and 5.0% for South East Towns. There is no category provided for places such as Camden Town which would be classified as Inner London. We would expect prime Camden Town offices to sit between the yields for the City Prime and South East Town; however, in view of the disadvantages of the proposed offices (especially being mostly lower-ground/basement space), we would not categorise it as a prime office in spite of being new-build.

6.7 We have compiled and analysed local investment transactions, as detailed in **appendix three**. The yields achieved for the comparables in Appendix 3 include 4.8% for Instrument House which is a superior location, near King's Cross. Regarding the Centro Building, it is very close to the subject site and achieved a net initial yield of 4.9%; it is a converted warehouse offering Grade A accommodation. Given the attractiveness of 'trendy' offices in Camden, being a converted warehouse is more of an asset than a disadvantage.

6.8 We have recently been provided with advice from Crossland Otter Hunt in respect of offices on St Pancras Way, which is a superior location to the subject site; they recommended a 4.5% net yield for a new-build, prime office. Adjusting this estimate for the Bayham Street site's inferior location, and inferior (mostly lower ground) facilities, this suggests a net yield of circa 5.5% net yield (which would be circa 5.8% gross yield) appears reasonable.

Affordable workspace

6.9 The Council's policy requires 20% of the office space to be at 50% of Market Rent. This has been achieved by reducing the overall rent of the offices by 10%. Given the relatively low level of the Market Rents on the lower floors, it should be established by the Council whether this policy applies in this case. In addition, given that the end-users of the space will not directly benefit from this rent reduction (as they will be licensees) it is unclear how useful it will be for this type of serviced office/hub arrangement.

7.0 PROPOSED HOTEL VALUES

Capital value

7.1 This 61-room hotel is valued at £240,000 per key (i.e. per room) based on specialist advice received from White Bridge Hospitality. This totals £14.6m. Their report is highly detailed and provides market analysis together with relevant comparable sales evidence. The price of £240,000 per key is close to some other hotel sales including the Travelodge Tower Bridge (£248,000) and is higher than the Doubletree Ealing sale. The Travelodge Union Street in Southwark was £279,000 but this reflects the exceptionally low yields achieved for this type of hotel, let to a major national budget operator.

7.2 Also, in respect of a recent scheme (2016) that we were involved in in Farringdon, we agreed that a hotel due to be operated by Whitbread was realistically priced at £225,000 per room, although this is likely to be higher today following market growth. Key comparables in that case were:

- **62-68 York Way, N1:** granted planning permission in 2014 for a 408 room hotel and 316m^2 retail in Kings Cross, part completed, to be tenanted by a new company with a guarantee from Whitbread Group, £3.5m per annum including three sublet units, lease spans 26 years with 1 year rent free, rent subject to 0-4% cpi uplifts payable every five years from the sixth year, equating to a capital value of **<u>£200,000 per key</u>**.

- **Spitalfields, Brick Lane, E1:** forward sale was agreed for a 189 bedroom 'hub' hotel let to Premier Inn Hotels Ltd with Whitbread as a guarantor, sold 14th October 2014 for £33.6m (**<u>£185,000 per key</u>**), due for completion March 2016.

7.3 We were recently involved in a hotel scheme on St Pancras Way (the 'Ugly Brown Building' site. This is a superior hotel location given it proximity to Kings Cross. The price per key that we agreed to was £383,000, based on detailed market evidence. This is an 87-room hotel, which is a more efficient size than the proposed hotel.

7.4 Thus based on comparable sales analysis (i.e. making a direct comparison to sales rates per room) the capital value adopted appears reasonable, but we have also consider the investment method followed by Whitebridge and looked at the income and yield assumptions adopted.

Capitalisation Rate (Yield)

7.5 White Bridge make the following comments regarding yields:

Arguably the most risk-free hotel investment in the world would be a budget hotel in central London leased to an operator with a strong covenant (such Premier Inn with a Whitbread plc covenant). These are typically selling off yields in the region of 3.75% to 4.5%. Lower yields are achieved in major gateway cities (eg London, Paris, New York), but only for a very limited number of trophy properties with world renowned reputations.

b) At present, hotels managed under management contract by internationally branded operators in most large international cities will typically sell off yields in the range of 6% to 9%, depending on their location and the stability of demand within that given city…

c) Thus, for the purposes of this project, we have assumed a risk premium above that indicated in a) above and below that indicated in b) above to allow for the project's simple concept and location within Camden, on the edge of Central London. We have balanced this with a degree or perceived risk that is inherent in any new development related project.

7.6 The current plan is, we understand, for the applicant to secure a Third Party Operator for the hotel, and this is expected to be a non-branded operator, which compared to a branded operator does typically lead to higher yield when selling in the investment market. There is uncertainty at this stage over the precise approach the applicant will take. But in view of the reasonably small size of the hotel it is realistic to assume that it will be unlikely to secure a large, branded operator. In this context the capitalisation rate (yield) of 5.0% is realistic. The yield evidence provided in White Bridge's report shows a yield of 5.3% for mid-market hotels in Central London, based on advice provided by six key consultancy firms active in the hotel market.

7.7 Yield evidence include sale at a 4.48% yield of the Intercontinental Park Lane and 4.50% for Intercontinental Westminster, both of which are in superior locations thus the 5.0% adopted by GL Hearn is reasonable in this context.

Hotel Income

7.8 The assumptions used for the hotel are:

- Average daily room rate of £112
- Food & beverage of £456,475
- Occupancy rate of 83%

7.9 These are discussed in detail be White Bridge. The occupancy rate compares to a rate of 84.9% estimated by hotel specialists the Hotel Management Company in respect of a hotel scheme in Shaftsbury Avenue that we have recently been involved in, in which the estimate was based on local market occupancy rates. A marginally lower rate is realistic for the Bayham Street hotel as Shaftsbury Avenue is a more prime, West End location.

7.10 The daily room rate compares to the local hotels set out by White Bridge. We have made a comparison to some other mid-market hotels:

- York & Albany, NW1 7PS – it has double and superior double rooms for £175 and £250 per night respectively. This is currently very similar, at £175 and £255 per night respectively, and the minor increase may not necessarily represent a general inflation of rates but rather month-to-month variation.
- Holiday Inn London Camden Lock, NW1 7BY - double and superior rooms for £199 and £230 respectively per night.

7.11 However, Average Daily Room rates do not always match the advertised room rates. Making deductions to the rack rates for VAT, for corporate discounts bookings and fluctuations in rates over the year, gives a total discount to reach average daily rates.

7.12 A mid-market hotel at the Camden Methodist Church has an estimated ADR of £137. Most of the rooms (41 in total) are small rooms of under 16 sq m, thus would not be expect to secure very high room rates. The ‘matrix’ of pricing proved by White Bridge does clearly indicate that the ADR they have adopted is suitable for this hotel, given its positioning within the wider London hotel market.

Hotel operating costs

7.13 A detailed breakdown of the running costs is provided by White Bridge:

	Amount (GBP)	Ratio	PAR (GBP)	POR (GBP)
Revenue				
Rooms	2,067,045	73.9%	33,886	111.57
Food	456,475	16.3%	7,483	24.64
Beverage	198,791	7.1%	3,259	10.73
Telephone	18,528	0.7%	304	1.00
Spa/leisure	-	0.0%	-	-
Other operated departments	55,583	2.0%	911	3.00
Rental & other income	-	0.0%	-	-
Total revenue	2,796,421	100.0%	45,843	150.93
Departmental Expenses				
Rooms	466,451	22.6%	7,647	25.18
Food & beverage	521,521	79.6%	8,550	28.15
Telephone	17,487	94.4%	287	0.94
Other operated departments	35,202	63.3%	577	1.90
Total Departmental Expenses	1,040,662	37.2%	17,060	56.17
Total departmental income	1,755,760	62.8%	28,783	94.76
Undistributed operating expenses				
Administration & general	229,746	8.2%	3,766	12.40
Sales & marketing	109,800	3.9%	1,800	5.93
Property operation & maintenance	130,000	4.6%	2,131	7.02
Utilities	109,800	3.9%	1,800	5.93
Total undistributed expenses	579,346	20.7%	9,497	31.27
Gross Operating Profit (GOP)	1,176,413	42.1%	19,285	63.50
Management Fees				
Base fees	83,893	3.0%	1,375	4.53
Incentives fees	109,252	3.9%	1,791	5.90
Total Management Fees	193,145	6.9%	3,166	10.42
Income Before Fixed Charges (IBFC)	983,269	35.2%	16,119	53.07
Fixed charges				
Property taxes	109,800	3.9%	1,800	5.93
Insurances	61,000	2.2%	1,000	3.29
Total fixed charges	170,800	6.1%	2,800	9.22
Net Operating Income (NOI)	812,469	29.1%	13,319	43.85
FFE replacement reserve	83,893	3.0%	1,375	4.53
Adjusted Net Operating Income (ANOI)	728,576	26.1%	11,944	39.32

7.14 This covers all the areas of expenditure that we would expect for a hotel of this nature. The total annual costs are £2.07m which is **£34,033 per room**. In order to sense-check the overall expenditure, we have made comparisons with total operating costs at other schemes. A hotel valuation that we undertook for Fulham Town Hall with the assistance of hotel specialist Melvin Gold Consulting, showed a £105,000 per room operating cost which is like-for-like with the above-cited operating costs for the proposed hotel (i.e. all costs except property taxes and insurance). This much higher rate reflects the more upmarket nature of the proposed Fulham Town Hall hotel; the main cause of this disparity is the difference in food & beverage expenses as the Fulham scheme will have a high quality restaurant open to the public, so by applying the same ££ cost per room for Food to Fulham as has been adopted for Bayham Street, this reduces Fulham's overall operating cost to £72,000 per room. All the individual cost items, including the admin, property maintenance and sales/marketing, are at low rates for the Bayham Street scheme. The Fulham Town Hall scheme is a very similar size, at 62 rooms, and indicates that White Bridge's operational costs are at a suitable level for a mid-market hotel.

7.15 For a budget hotel we were involved with in Hounslow, the total operating costs are only £9,000, which is largely due to the exceptionally low Food budget of £3,444 per room. A more similar scheme is the proposed hotel development on Shaftsbury Avenue. This hotel showed total operating costs of £47,000 per room, on a like-for-like basis with the examples above. This is a more upmarket hotel than the Bayham scheme, and has a spa which adds to the operating costs.

7.16 Another scheme we have been involved in is the proposed hotel at 2-6 St Pancras Way (the 'Ugly Brown Building' site), which is proposed to be a mid-market hotel. The estimated total operating cost (except property taxed and insurance) is £37,850 per room; this is the best comparator to the proposed Bayham Street hotel, and has a very similar level of costs. In this context, the lower overall cost of £34,033 per room appears to be realistic.

7.17 Taking into account the specifics of this scheme, including the extensive food & beverage facilities, the level of operating costs appear to be reasonable, based on our cross-check against other hotel schemes that we have been involved in.

BPS Chartered Surveyors

Appendix One

7abc Bayham St, Camden NW1 0EY

Cost Review by Neil Powling FRICS

1 SUMMARY

1.1 The building comprises a basement, lower ground floor, ground floor and four floors above: a 7 storey building – mainly hotel with 690m² of offices. For benchmarking purposes we have treated the entire building as hotel.

1.2 Although the viability report refers to the co-working office operator undertaking their own fit out before starting operations – which would imply a shell & core only until the operator is appointed, the estimate has been prepared on the basis of fit out to office areas. We have benchmarked on the same basis.

1.3 Our benchmarking yields an adjusted benchmark rate of £4,054/m² that compares to the Applicant's estimate of £4,146/m² a difference of £92/m² (£279,700). Despite this difference in benchmarking and based on consideration of the detail in the cost estimate, we consider the costs to be reasonable.

2 METHODOLOGY

2.1 The objective of the review of the construction cost element of the assessment of economic viability is to benchmark the Applicant's costs against RICS Building Cost Information Service (BCIS) average costs. We use BCIS costs for benchmarking because it is a national and independent database. Many companies prefer to benchmark against their own data which they often treat as confidential. Whilst this is understandable as an internal exercise, in our view it is insufficiently robust as a tool for assessing viability compared to benchmarking against BCIS. A key characteristic of benchmarking is to measure performance against external data. Whilst a company may prefer to use their own internal database, the danger is that it measures the company's own projects against others of it's projects with no external test. Any inherent discrepancies will not be identified without some independent scrutiny.

2.2 BCIS average costs are provided at mean, median and upper quartile rates (as well as lowest, lower quartile and highest rates). We generally use mean or occasionally upper quartile for benchmarking. The outcome of the benchmarking is little affected, as BCIS levels are used as a starting point to assess the level of cost and specification enhancement in the scheme on an element by element basis. BCIS also provide a location factor compared to a UK mean of 100; our benchmarking exercise adjusts for the location of the scheme. BCIS Average cost information is available on a default basis which includes all historic data with a weighting for the most recent, or for a selected maximum period ranging from 5 to 40 years. We generally consider both default and maximum 5 year average prices; the latter are more likely to reflect current regulations, specification, technology and market requirements.

2.3 BCIS average prices are available on an overall £ per sqm and for new build work on an elemental £ per sqm basis. Rehabilitation/conversion data is available an overall £ per sqm and on a group element basis ie. substructure, superstructure, finishings, fittings and services – but is not available on an elemental basis. A comparison of the applicants elemental costing compared to BCIS elemental benchmark costs provides a useful insight into any differences in cost. For example: planning and site location requirements may result in a higher than normal cost of external wall and window elements.

2.4 If the application scheme is for the conversion, rehabilitation or refurbishment of an existing building, greater difficulty results in checking that the costs are reasonable, and the benchmarking exercise must be undertaken with caution. The elemental split is not available from the BCIS database for rehabilitation work; the new build split may be used instead as a check for some, but certainly not all, elements. Works to existing buildings vary greatly from one building project to the next. Verification of costs is helped greatly if the cost plan is itemised in reasonable detail thus describing the content and extent of works proposed.

2.5 BCIS costs are available on a quarterly basis – the most recent quarters use forecast figures, the older quarters are firm. If any estimates require adjustment on a time basis we use the BCIS all-in Tender Price Index (TPI).

2.6 BCIS average costs are available for different categories of buildings such as flats, houses, offices, shops, hotels, schools etc. The Applicant's cost plan should ideally keep the estimates for different categories separate to assist more accurate benchmarking. However if the Applicant's cost plan does not distinguish different categories we may calculate a blended BCIS average rate for benchmarking based on the different constituent areas of the overall GIA.

2.7 To undertake the benchmarking we require a cost plan prepared by the applicant; for preference in reasonable detail. Ideally the cost plan should be prepared in BCIS elements. We usually have to undertake some degree of analysis and rearrangement before the applicant's elemental costs can be compared to BCIS elemental benchmark figures. If a further level of detail is available showing the build-up to the elemental totals it facilitates the review of specification and cost allowances in determining adjustments to benchmark levels. An example might be fittings that show an allowance for kitchen fittings, bedroom wardrobes etc that is in excess of a normal BCIS benchmark allowance.

2.8 To assist in reviewing the estimate we require drawings and (if available) specifications. Also any other reports that may have a bearing on the costs. These are often listed as having being used in the preparation of the estimate. If not provided we frequently download additional material from the documents made available from the planning website.

2.9 BCIS average prices per sqm include overheads and profit (OHP) and preliminaries costs. BCIS elemental costs include OHP but not preliminaries. Nor do average prices per sqm or elemental costs include for external services and external works costs. Demolitions and site preparation are excluded from all BCIS costs. We consider the Applicants detailed cost plan to determine what, if any, abnormal and other costs can properly be considered as reasonable. We prepare an adjusted benchmark figure allowing for any costs which we consider can reasonably be taken into account before reaching a conclusion on the applicant's cost estimate.

2.10 We undertake this adjusted benchmarking by determining the appropriate location adjusted BCIS average rate as a starting point for the adjustment of abnormal and enhanced costs. We review the elemental analysis of the cost plan on an element by element basis and compare the Applicants total to the BCIS element total. If there is a difference, and the information is available, we review the more detailed build-up of information considering the specification and rates to determine if the additional cost appears justified. If it is, then the calculation may be the difference between the cost plan elemental £/m² and the equivalent BCIS rate. We may also make a partial adjustment if in our opinion this is appropriate. The BCIS elemental rates are inclusive of OHP but exclude preliminaries. If the Applicant's costings add preliminaries and OHP at the end of the estimate (as most typically do) we add these to the adjustment amounts to provide a comparable figure to the Applicant's cost estimate. The results of the elemental analysis and BCIS benchmarking are generally issued as a PDF but upon request can be provided as an Excel spreadsheet.

3 GENERAL REVIEW

3.1 We have been provided with and relied upon the Financial Viability Assessment issued by GL Hearn 17th August 2018 for Camden Lifestyle (UK) Ltd including at Appendix IV the Feasibility Study Nr1 Rev 2 issued by Gleeds 6 Aug 2018.

3.2 The feasibility study (estimate) is based on current market levels at 6th August 2018 (3Q2018). Our benchmarking uses current BCIS data which is on a current tender firm price basis. The BCIS all-in Tender Price Index (TPI) for 3Q2018 is 313 and for 4Q2018 315 – both figures are forecasts.

3.3 The estimate includes an allowance of 16.3% for preliminaries. Given the current tender market, the location, site constraints and the design details we consider this addition reasonable. The allowance for overheads and profit (OHP) is 5.5%; we also consider this reasonable.

3.4 The inclusion for risk in the estimate has been excluded from the construction cost in the appraisal and an allowance for contingencies made of 5% which we consider reasonable. All the % figures are based on a calculation of a conventional arrangement of the sums in the analysis.

3.5 We have extracted the cost information provided by the Applicant into a standard BCIS/NRM format to facilitate our benchmarking.

3.6 We have downloaded current BCIS data for benchmarking purposes including a Location Factor for Camden of 129 that has been applied in our benchmarking calculations.

3.7 The building comprises a basement, lower ground floor, ground floor and four floors above: a 7 storey building – mainly hotel with 690m² of offices. For benchmarking purposes we have treated the entire building as hotel.

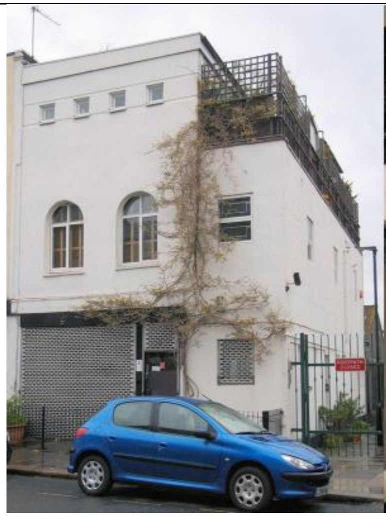
3.8 Although the viability report refers to the co-working office operator undertaking their own fit out before starting operations – which would imply a shell & core only until the operator is appointed, the estimate has been prepared on the basis of fit out to office areas. We have benchmarked on the same basis.

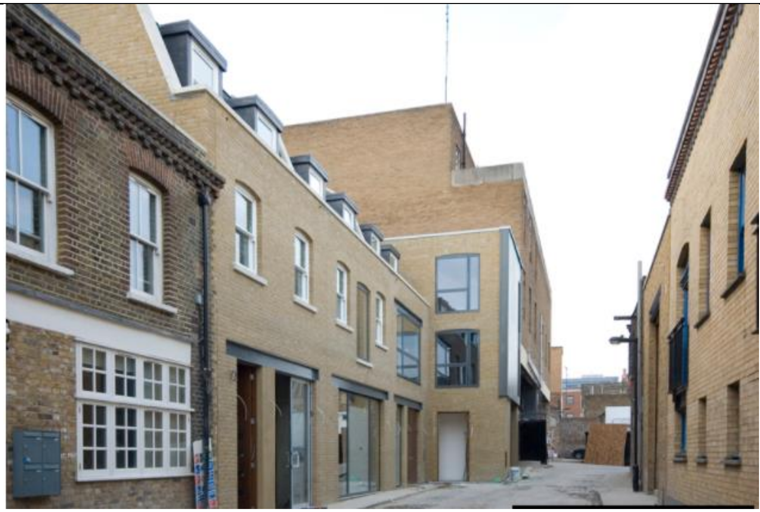
3.9 Our benchmarking yields an adjusted benchmark rate of £4,054/m² that compares to the Applicant's estimate of £4,146/m² a difference of £92/m² (£279,700). Despite this difference in benchmarking and based on consideration of the detail in the cost estimate, we consider the costs to be reasonable.

BPS Chartered Surveyors
Date: 26th October 2018

Appendix Two

<u>BPS analysis of recent lettings – comparison to 7abc Bayham Street site</u>

Fusion House, 5 Rochester Mews, NW1 9JB Part 1st floor let January 2017 £42.50 per sq ft		New building completed in 2010. Located to the north of the subject site at Bayham Street. This is arguably a marginally less attractive location as further from Camden High Street New building (constructed 2010). Grade A space. With air conditioning. Full height double-glazed windows. Underground parking up to 5 cars.
5 Castle Road, NW1 8PR Ground floor let in October 2016 for £27.23 per sq ft	  	Attractive period building. Located north of subject site. Offices have reasonable specification internally. Good natural light, as shown by pictures as full height windows. No car parking. This is an less attractive location, thus we would expect higher rents at 7abc Bayham Street.

Kings Studios, 43-47 Kings Terrace, NW1 0JR Ground and 1st floor (part) let in August 2016 for £39.88 per sq ft		Building constructed in 2010, providing media-style, 'trendy' offices Similar quality of location to subject site. It is adjacent to Camden High Street. Good natural light. No parking but close to Tube.
Centro (block 4), 20-23, Mandela Street, London, NW1 0DU Let for £60 per sq ft in September 2018		Media-style offices. Recently comprehensively refurbished. Very close to subject site. Comfort cooling.

128, Albert Street, Parkway, London, NW1 7NE Let for £55.00 per sq ft in February 2018		Second-hand Grade offices. Air conditioning available. Former warehouse converted to offices. This is to the west of the subject site, similar in term of quality of location and access to the high street and other amenities.

Appendix Three

BPS analysis of office investment sales evidence – comparison to 7abc Bayham Street site

Address	Sale details	Description & comments
The Centro Building, 39 Plender Street, NW1	Sold in Apr-18 for £76.5m 4.90% net initial yield	84,855 sq ft of office space let to tenants including Hugo Boss, French Connection and F45 Fitness. Very good specification and condition. Vacant floor space totalled 12,286 sq ft. The average current passing rent equates to £53.70 psf.
Atelier House, Selous House & Centro 3,4 &5, 64 Pratt Street NW1	Sold in Jan-18 for £109m, 4.20% net initial yield.	131,000 sq ft of multi-let office space. 21,000 sq ft of space is currently vacant and undergoing refurbishment. The average current passing rent equates to £44.70 psf.
106-110 Kentish Town Road NW1	Sold in Jun-17 for £25.3m 4.30% net initial yield	35,352 sq ft of multi-let office space. Recently refurbished. Very good specification and condition. Vacant floor space totalled 4,600 sq ft. With the average passing rent at £33.67 psf.

Address	Description	Date	Transactional Information
First Avenue House, 42-49, High Holborn, WC1V 6NP	Entire office building 112,274 sq ft of office accommodation Let in its entirety to the First Secretary of State until September 2038 with fixed rental uplifts of 2.5% per annum Purchased by the Japanese firm Sumitmo Mitsui Trust Bank Property is close to Chancery Lane underground station.	01/03/18	£154,000,000 Yield: 3.46%
Instrument House, 207-215 King's Cross Road, WC1X 9DN	Newly refurbished office block Fully let to four tenants for a further 5.6 years (3.5 years to break option) Purchased by a Hong Kong investor Totals 12,200 sq ft	01/12/17	£15,000,000 Yield: 4.8%
Mitre House, 160, Aldersgate Street, EC1A 4DD	Purchased by German fund manager Union Investment and let to law firm DLA Piper's as their new City headquarters Lease terms agreed in February 2018 with expiration in 2038 The property was extensively refurbished before sale Comprises 149,999 sq ft of space	01/11/17	£220,000,000 Yield: 4.5%
Lacon House, 84, Theobalds Road, EC1X	Large eight storey office block comprising 208,033 sq ft New-build and delivered to Grade	01/09/17	£285,000,000 Yield: 4.48%

8RW	A standard with a large communal terrace, a shared 6,000 sq ft reception area, a gym at ground floor and cycle facilities, such as parking and bike maintenance areas		
Churchill House, 142-146, Old Street, EC1V 9BW	Attractive office building refurbished in 2014 and arranged over lower ground, ground and five upper floors (26,738 sq ft) Multi-let to 5 tenants including Maplin Electronics Limited and Seedrs Limited Total passing rent of £1,194,880 (£44.69psf) but with a suggested ERV of £1,616,067 (£60.44psf) Benefits from planning permission for the construction of a sixth floor of office space with terraces Close to Old Street underground station	01/07/17	£25,980,000 Yield: 4.31%