Independent Viability Experts

FAO Ms Maxine Simmons
Planning Officer
South Holland District Council

Sent by email only

David Newham MRICS
Director
CP Viability Ltd
T: 01937 360 131
M: 07947 120 953
E: davidnewham@cpviability.co.uk

Our ref: DN-07
Your ref: H16-0523-22
Date: 15th December 2022

Dear Ms Simmons,

PROPERTY ADDRESS: Land off Roman Bank Spalding PE11 2HN
INSTRUCTING BODY: South Holland District Council
APPLICANT: Scenic Homes Ltd



Further to your instruction dated 30th November 2022, we are pleased to report as follows.

1. Property Overview

1.1. The property is located on the north eastern fringe of Spalding town centre, around a mile from the natural centre of the town. It is on the outskirts of the residential areas with commercial buildings to the west and north west and Springfields Outlet Shopping and Leisure centre to the north east. Main road access to the property is via Roman Bank which in turn links with the A151 (Holbeach Road) a main route through the town. The A16 can be accessed around 750m to the east providing links to Boston approx. 14 miles to the north and Peterborough approx. 20 miles to the south. The nearest rail connection is Spalding train station, circa 1 mile to the south west of the subject property, with services to Peterborough, Doncaster and Lincoln.

1.2. More specifically, the subject property is situated on the north west side of Roman Bank, behind a block of flat named Windmill Court. The site is bounded to the north west by the River Welland, to the south west by an area of currently unused land (subject to planning application H16-0138-17), to the south east by Roman Bank and to the north east by a block of flats named Lansdowne Court. Access is via a single point on Roman Bank. New build semi- detached housing has been built on the opposite side of Roman Bank (immediately beyond which there is a Lidl Supermarket) and on the opposite side of the River Welland there are commercial buildings housing print companies, factories and warehouses.

1.3. The property comprises an overgrown area of scrub land with a concrete access road and parking area to the front (eastern portion) of the site. It is generally level and irregular in shape. According to the application form submitted on behalf of the applicant company, the site extends to 0.08 Ha (0.21 acre) on a gross basis.

1.4. In terms of planning history, the following application is noted:

> **H16-1031-07** "*Residential Development of 18 flats and associated works (outline H16-0411-05)*" This was approved in September 2007.

1.5. However, this forms part of a wider site, part of which has now been developed as flats (known as Windmill Court).

1.6. In terms of specifically the subject site, the following application was submitted:

> **H16-1062-17** "*Residential Development of 12 one-bedroom apartments flats*" This was approved in November 2017.

1.7. Upon the instruction of the Council, in July 2018 we undertook a viability review of the scheme. At the time, the applicant submitted a viability appraisal indicating that the scheme was unable to support any affordable housing. Based on our review, we concurred with the applicant's findings and agreed that the scheme was unable to support any affordable housing.

1.8. The current application is for:

- **H16-0523-22 -** *"Residential Development – 12 one bedroom apartments"*

1.9. This envisages the development of a single 3 storey block of 12 one bedrooms apartments with associated parking.

1.10. Studio 11 Architecture ("S11") has submitted a "Financial Viability Report" on behalf of the applicant company in the form of a letter dated 26th October 2022, including a summary appraisal which gives the following schedule of accommodation:

Type	Units	Av Sq ft	Total sq ft
Apartment	12	450	5,400
Total	**12**		**5,400**

2. Scope of Assessment and General Assumptions

2.1. S11 letter and appraisal summary considers a single non-target policy compliant scenario based on no affordable housing contribution or other planning policies. Adopting a fixed land value of £100,000, their appraisal generates a developer profit equivalent to 7.54% on revenue. S11 conclude that "Given the limited profit in the scheme we are of the opinion that it is incapable of supporting any affordable housing contributions".

2.2. We have been instructed to provide an independent viability assessment of the redevelopment of the subject site for the proposed use, reviewing the scenario submitted by S11 and addressing the issue of its capacity to deliver planning policy contributions.

2.3. In accordance with the RICS Financial viability in planning: conduct and reporting 1st Edition (May 2019) we can confirm that in completing this instruction CP Viability Ltd have acted with objectivity, impartiality, without interference and with reference to all appropriate available sources of information.

2.4. In accordance with the RICS Financial viability in planning: conduct and reporting 1st Edition (May 2019) we can confirm that prior to accepting this instruction we undertook a conflict of interest check. It is stressed that as an organisation we only provide independent viability reviews upon the instruction of Local Authorities and therefore can guarantee that we have not provided viability advice on behalf of the applicant for this scheme. Within this context and having undertaken a review we are unaware of any conflict of interest that prevents CP Viability from undertaking this instruction. If, at a later date, a conflict is identified we will notify all parties to discuss how this should be managed.

2.5. In accordance with the RICS Financial viability in planning: conduct and reporting 1st Edition (May 2019) we can confirm that the fee agreed to undertake this review is a fixed rate (covering the elements set out in our fee quote / terms of engagement) and is not performance related or a contingent fee.

2.6. In accordance with the RICS Financial viability in planning: conduct and reporting 1st Edition (May 2019) we can confirm that CP Viability Ltd is not currently providing ongoing advice to South Holland District Council in area-wide financial viability assessments to help formulate policy.

2.7. We have assessed the viability of the scheme as at 15th December 2022.

2.8. We have relied on the information provided to us by the instructing body and the applicant and in particular information publicly available through the Council's planning portal website.

2.9. We have not met either of the Instructing Body or the applicant/developer and subsequently have not partaken in any negotiations regarding the scheme.

2.10. In accordance with the RICS "Assessing viability in planning under the National Planning Policy Framework 2019 for England (Guidance Note 1st Edition, March 2021), our appraisal assumes a hypothetical landowner and a hypothetical developer. The intention of a viability assessment is therefore to identify the approach a 'typical' or 'average' developer / landowner would take to delivering the site for development. A viability assessment does not therefore seek to reflect the specific circumstances of any particular body (whether landowner or developer).

2.11. In undertaking our appraisals, we have utilised ARGUS Developer. This is an industry approved cash-flow model, designed specifically residual appraisals. This report reflects the independent views of CP Viability, based on the research undertaken, the evidence identified and the experience of the analysing surveyor.

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3. S11 Appraisal – Summary

3.1. As indicated above, S11 have submitted their "Financial Viability Report" and appraisal summary on behalf of the applicant company in the form of a letter dated 26th October 2022. S11 consider only 1 scenario, which excludes any planning policies.

3.2. To summarise their assumptions, we have categorised the costs provided under what we consider to be the most common sections of a viability appraisal. For example, all costs which we believe relate to the basic construction of a dwelling (including a contractor's margin or developer's overhead) have been allocated under "Apartment/commercial block". This categorisation approach allows us to undertake a comparison between the subject scheme and other developments we have assessed. We would summarise this scenario as follows:

Gross Development Value (Revenue)

Type	No.	Av £ per sq ft	Total
Market Value apartments	12	£222	£1,200,000
Total			**£1,200,000**

Gross Development Cost (Outgoings)

Type	Notes	Total
Apartment construction	£133.58 per sq ft (GIA 5,400 sqft)	£721,354
Externals	16.05% of build costs	£115,800
Abnormal costs	Various	£91,000
Professional fees	7.48% of build costs	£64,975
Sales legal fees	£950 per dwelling	£11,400
Benchmark land value		£100,000
Acquisition costs	Legal fees	£5,000
Total		**£**

3.3. Based on S11's assumptions, the scheme generates a developer profit of £90,471 equivalent to rate of return on revenue of 7.54%. In the light of this, S11 conclude that: "…this application has demonstrated that the development cannot deliver any financial contributions/affordable housing contributions…the applicant has indicated that they are willing to accept that level of return on the project given that they currently own the land."

4. CP Viability's appraisal

Gross Development Value (Revenue)

4.1. In their supporting letter S11 indicate that, "It is intended that the whole completed development is sold to a private rental company for £1,200,000". The scheme is not therefore a typical piecemeal disposal it is a bulk investment sale to a single purchaser. Typically, in these scenarios a deal is agreed prior to commencement of construction.

4.2. To test whether the adopted investment value is reasonable or not it is necessary to consider the underlying rental values of the completed apartments. In terms of the Spalding apartment market, we note the following currently available to let:

- Westlode Street, Spalding: 1 bed flat available for £625 per calendar month
- Double Street, Spalding: 1 bed flat available for £550 per calendar month
- Double Street, Spalding: 1 bed flat available for £525 per calendar month

4.3. We also note that in the adjacent existing 3 storey apartment building (known as Windmill Court) there have previously been 1 bed flats marketed to let at £480 to £525 per calendar month.

4.4. Adopting a bullish approach, and allowing for a new build premium, we have assumed an average rental of £650 per calendar month across the 12 flats. This equates to a total gross aggregate rental income of £100,800 per annum. Allowing a 20% discount to cover running costs (such as voids, management, letting fees etc) this gives a total net rental income of £74,880 per annum.

4.5. To generate an investment value of £1.2million, including an allowance for purchaser's costs, this would mean an investment yield of just under 6%. This is considered to be reasonable given the nature of the scheme.

4.6. From an investment perspective, S11 suggested scheme revenue of £1.2million is therefore deemed to be reasonable.

4.7. In addition, and to ensure a robust review, we have also considered whether a 'break up' sale of the scheme (i.e. the individual flats are sold separately) would generate any higher level of revenue. Based on £1.2million this is equivalent to an average value of £100,000 per flat.

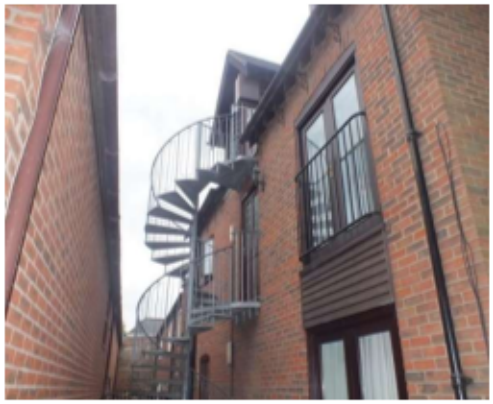
4.8. By way of evidence, we have initially reviewed Land Registry new build sales data for apartments in the same postcode area 'PE11' as the subject site since January 2020. However, there is no new build transactional evidence within this area during this period.

4.9. Given the lack of new build transactional evidence, we have also researched new build flats currently available for sale within Spalding. However, again there is currently no available evidence.

4.10. In the absence of any discernible new build evidence, we have subsequently considered 'second-hand' flat sales within a circa 1 mile radius of the subject site which have sold within the last 12 months and also flats currently available for sale. We note the following:



- 9 River Court, Spalding
- Around 1 mile south west of the subject site, close to the river.
- 2 bed converted apartment.
- 570 sq ft.
- Sold in Jun 22 for £99,950 (£175 psf).
- For smaller, 1 bed flats S11 allow £100,000, which compares favourably.



- Flat 7, The Quay, Double St, Spalding
- Around 1 mile south west of the subject site, close to the river.
- Older, purpose built 1 bed apartment.
- 420 sq ft.
- Sold in Mar 22 for £60,000 (£143 psf).
- For 1 bed flats S11 allow £100,000, which compares favourably.



- 2, Georgian Court, Spalding
- Around 1 mile south west of the subject site, close to the river.
- Purpose built (around 2001) 1 bed apartment.
- 495 sq ft.
- Sold in Dec 21 for £72,500 (£146 psf).
- For similar sized 1 bed flats S11 allow £100,000, which compares favourably.

4.11. In terms of apartments currently available for sale, we note 7 x 1 bed flats available in the market, ranging from £67,750 to £89,995. However, all 7 are retirement flats and subsequently not considered to be directly comparable to the subject scheme (as they carry more significant service charges, ground rents, are only available to a restricted market etc).

4.12. As for economic conditions, at the current time the market is experiencing a high level of uncertainty and volatility. Over recent weeks the residential market has experienced a significant adjustment. The Bank of England base rate has recently been increased to 3%, compared to 0.5% at the start of 2022. The knock-on effect of this and the government's announcement is that mortgage providers have significantly increased the cost of mortgage products, with rates pushing out towards 6.5% (compared to sub 2.5% as at Jan 22). The sharp increase in monthly repayments, combined with the ongoing cost of living / energy crisis, has meant a greater pressure on affordability.

4.13. By way of an example as to the impact this has on affordability, for a sale price of £200,000, with a 10% deposit this would mean a mortgage of £180,000. In the summer 2022 mortgages were available at around 2.5%. Assuming a 25 year mortgage period, this equates to a monthly repayment of £814. As at the time of writing, mortgages have increased to around 6.5%. On the same criteria this would means a mortgage repayment of £1,229 per calendar month, a circa 50% increase in the monthly payment. Furthermore, additional rises in interest rates are expected in the coming weeks in an attempt to temper inflation. If mortgage rates increase to say 8%, the monthly repayment would be £1,405. This level of increase in mortgage costs will significantly impact on purchaser affordability, which in turn will reduce demand. The 'knock-on' effect is a reduction in property prices.

4.14. In light of these market conditions, and whilst these are nothing but early predictions, some commentators are predicting that values could fall by circa 5% to 15% in 2023. This, it is stressed, is yet unproven, however it does highlight current market sentiment.

4.15. From a valuation perspective, there is subsequently significant uncertainty as to how values will perform going forward. Current signs are that values will start to fall (as asking prices are reduced to try and drive sales). This has yet to manifest itself through clear transactional data, although we are noticing asking prices being reduced across the marketplace.

4.16. Having reviewed the (limited) market evidence it appears there is no tangible market evidence to suggests that in excess of £100,000 per apartment could be achieved if the flats were sold individually.

4.17. Based on the above comments, we conclude that it is reasonable to adopt a total scheme revenue of £1.2million in the appraisal.

Construction costs

4.18. S11 adopt the following construction costs in relation to the proposed scheme:

- Apartment build £133.53 per sq ft
- Externals £115,800 (16.05% of above costs)
- Abnormal works £59,500 (see below for further details)

4.19. For the purposes of this viability review we consider it appropriate to benchmark construction costs by using the Build Cost Information Service ("BCIS"), a cost database regularly used in the industry for establishing construction costs. Please note that BCIS rates include the contractor's overhead and preliminaries; however, it excludes external works costs, contingency, abnormal works costs and professional fees which consequently have to be allowed for separately if the BCIS rate is being applied.

4.20. We note the following current rates for new build apartments (3 – 5 storey), rebased to South Holland:

- Lower Quartile £1,370 per sq m (£127.27 per sq ft)
- Median £1,554 per sq m (£144.37 per sq ft)

4.21. S11's suggested rate (£133.58 per sq ft) therefore falls in between the lower quartile and the median BCIS rates. For a scheme of this nature and scale we would expect the build costs to be closer to the median rates and therefore S11's allowance compares favourably. In light of this, we see no justification for reducing S11's allowance and have subsequently adopted the same in our appraisal.

4.22. For what we consider to be standard or typical externals, the following are included within S11's appraisal:

Fencing	£13,000
Driveways / parking	£44,100
Street lighting	£7,500
Public open space	£5,000
Mains & services	£36,000
Water connection	£10,200

4.23. At £115,800 the external costs equate to 16.05% of the apartment construction cost. Typically, we would expect this figure to be in the region 10% for an apartment scheme of this scale. However, in this particular case, as discussed above, if anything the plot costs could be argued to be on the lower side of expectations in the current climate, therefore the externals are working from a lower figure (which pushes up the percentage rate when analyzing on this basis). Furthermore, we note that S11 do not appear to allow a contingency, which is commonly used (and accepted within the guidance) when testing viability. Taking int account these factors, and considering the wider cost allowances holistically, we conclude that the figures applied by S11 are broadly reasonable for the purposes of a viability review and have subsequently been accepted in our appraisal.

4.24. For what we consider to be abnormal works, the following are included in S11's assessment

Site clearance	£7,500
Surface water attenuation	£10,000
Piled foundations	£42,000
E/O private parking	£31,500

4.25. In terms of the extra-over private parking costs, together with the standard 'driveway' (which we have taken to mean parking space) allowance this equates to £5,400 per space. In our view, this is above expectations for providing parking spaces at the scheme. We would expect around £4,000 per space. We have subsequently reduced the 'extra-over' elements (which are not explained or justified) to £12,500. Overall this reduces the abnormal costs to £72,000.

4.26. In terms of the other abnormal cost items, we would stress that we are not Quantity Surveyors and are unable to provide a detailed review of these abnormal costings without third party input (which would have time / cost implications). However, to some degree the impact of abnormal costs can be offset in the land price (at least when determining viability). The Planning Practice Guidance ('PPG') on viability makes it clear that abnormal costs must be factored into the assessment of land value, with the implication being the higher the abnormal costs the greater the downward pressure on land value.

4.27. In practical terms, it is not the case that if abnormal costs go up by £100,000 per acre the land value will always decrease by £100,000 per acre, as the land value still has to be at a sufficient level to incentivise a landowner to release the site for development. For example, if a site has an existing use value as an agricultural field at £10,000 per acre and, after abnormal costs are deducted, a residential scheme can only deliver a land value of £15,000 per acre then this would not represent a sufficient incentive for a landowner to release the site for development. There still has to be some sort of suitable premium above the existing use value. However, it is reasonable that the burden of the higher abnormal costs on a development should not fall solely on the Council through a reduction in their planning policies. The principle that the land value must bear the most significant proportion of any abnormal costs is a sound one.

4.28. In short, changes in abnormal costs are of course significant. However, when assessing viability, they should be balanced against land value (which can serve to dampen the effect of abnormal costs on the overall viability outcome).

4.29. Having considered these factors, for the purposes of the modelling we have run our appraisal on the basis of our adjusted abnormal costs of £59,500, albeit on the basis that this is balanced with an appropriate level for the benchmark land value, as per the requirements of the Planning Practice Guidance.

Professional fees

4.30. S11's professional fees allowance is equivalent to 7.76% of our combined adjusted build costs.

4.31. To assess whether this is a reasonable allowance or not we have reviewed other viability appraisals we have received for similar developments (across the wider regions). In each case, we have identified the professional fees submitted to us by applicants in their own viability appraisals. Since Jan 2020 we have identified 8 similar scale apartment schemes, ranging from 12 to 18 units. Across this sample, the professional fees allowance submitted to us ranged from 3.88% to 15.75%, with a sample average of 9.55%. Based on this evidence, S11's allowance is not considered to be excessive (and if anything could be argued to be on the lower side of expectations). We have subsequently adopted the same in our appraisal.

Marketing / disposal fees

4.32. We note that S11 do not specifically allow for any disposal costs of the scheme (as an investment). It is assumed that is because the investment disposal fee has already been factored into the net sales price of the scheme. We have adopted this approach in our appraisal.

Finance

4.33. S11 do not appear to allow for any finance costs.

4.34. It is stressed that when testing viability, it is necessary to assume hypothetical developers and hypothetical landowners. In other words, the specific financial circumstances of individual parties are not reflected in the modelling, instead we have to assume the 'typical' developer's financial circumstance. In this regard, it is common practice to assume that a developer would require third party funding in order to build out the development.

4.35. However, in this particular case, the lack of finance costs is likely to be because the purchase price for the scheme would be forthcoming at Day 1 of the construction phase. In other words, there is no need for third-party funding because the purchaser of the investment would be effectively funding the construction of the scheme by paying for the scheme in advance of development.

4.36. We have subsequently adopted the same approach in our own appraisal and therefore excluded any finance costs.

Developer profit

4.37. For a scheme of this size and nature we believe it is appropriate to apply a profit margin expressed as a percentage of the revenue.

4.38. In our experience profit margins fluctuate depending on the nature of the scheme and the type of developer implementing the project. For a 'traditional' flat scheme (where apartments are sold individually), and only as a broad guide, we tend to see net profit margins in the region of 15% to 20% of revenue. This is also consistent with the Planning Practice Guidance: Viability which also refers to this range.

4.39. However, the risk profile attached to a Build to Rent scheme is different, because, unlike a 'traditional' apartment scheme where the units are sold individually and speculatively in the market place, the flats would be sold as a single entity to a single party, who may have been identified before construction works commence. This means that the risk profile is considerably lower when compared to apartments being sold on an individual basis. The Planning Practice Guidance on viability supports this, stating that "Alternative figures [from the 15% to 20% range] may also be appropriate for different development types".

4.40. For this scheme, where it is assumed, the project would be delivered as a Build to Rent asset, to reflect the lower associated risks we consider a 12.5% on revenue allowance to be appropriate (which equates to £150,000).

Benchmark Land value

4.41. The Benchmark Land Value ("BLV") attempts to identify the minimum price that a hypothetical landowner would accept in the prevalent market conditions to release the land for development. Whilst a relatively straightforward concept, in reality, it is open to interpretation and is generally one of the most debated elements of a viability appraisal. It is also often confused with market value, however the guidance stresses that this is a distinct concept and therefore is different to market value assessments.

4.42. The most recent guidance is detailed within the National Planning Policy Framework ('NPPF') and Planning Practice Guidance ('PPG'), as published on 24th July 2018 (and updated in May and September 2019). This provides a more up to date guide to undertaking viability assessments. One key area which the PPG specifically deals with is in relation to assessing BLV, stating the following (and setting out a clear methodology for arriving at a benchmark land value):

4.42.1. To define land value for any viability assessment, a benchmark land value should be established on the basis of the existing use value (EUV) of the land, plus a premium for the landowner. The premium for the landowner should reflect the minimum return at which it is considered a reasonable landowner would be willing to sell their land.

4.42.2. The EUV should disregard any hope value.

4.42.3. Benchmark land value should reflect the implications of abnormal costs, site specific infrastructure costs and professional site fees.

4.42.4. Benchmark land value should be informed by market evidence including current uses, costs and values wherever possible.

4.42.5. Where recent market evidence is used to inform assessment of benchmark land value this evidence should be based on developments which are compliant with policies, including affordable housing. Where this evidence is not available plan makers and applicants should identify and evidence any adjustments to reflect the cost of policy compliance. This is so that historic benchmark land values of non-policy compliant developments are not used to inflate values over time.

4.42.6. Under no circumstances will the price paid for land be a relevant justification for failing to accord with the relevant policies in the plan.

4.42.7. Alternative Use Value of the land may be informative in establishing benchmark land value. However, these should be limited to those uses which have an existing implementable permission for that use. Valuation based on AUV includes the premium to the landowner. If evidence of AUV is being considered the premium to the landowner must not be double counted.

4.43. In other words, the Council should not subsidise (through a loss of planning policy contributions) any overbid made when acquiring the site. Any overbid (or indeed underbid) for a site should therefore be disregarded when considering the BLV. As part of the process of reviewing viability it is down to the assessor to determine whether a price paid is an appropriate figure (or not) to use as a BLV.

4.44. In their submission, S11 simply state that: "The application site was purchased for a land value of £105,000 including legal costs."

4.45. In terms of the approach, the guidance is clear under no circumstances can the purchase price agreed be used as a justification for reducing or removing planning policies. Instead, the guidance indicates that when testing viability, it is necessary to establish the benchmark land value, with the main method being through the 'existing use value plus premium' approach.

4.46. As discussed above in Section 1, we previously undertook a viability assessment in July 2018 as part of a previous planning application. At the time, we concluded that the benchmark land value should be based on a relatively modest sum to reflect this being effectively 'scrub' land. We referred to a range of £25,000 to £50,000 at that time.

4.47. For the purposes of this update, we again consider that the underlying benchmark land value should reflect the 'scrub' land value of the site. However, since our last assessment was undertaken in July 2018, the Planning Practice Guidance: Viability was introduced and this clearly states that it is necessary to provide an incentive to a landowner over the underlying existing use value in order to encourage the site to be released for development. In light of this, our view is that the upper end of our previously identified range (£50,000) would be a sufficient incentive for a landowner to release this site for development. We have subsequently used this as the benchmark land value in our appraisal.

5. Overall conclusions

5.1. Please see attached our appraisal. With nil onsite affordable housing the scheme generates a residual land value of £72,258. As this is above our benchmark land value of £50,000 this shows that the scheme is viable with a surplus of £22,258.

5.2. In summary, we find that the scheme is able to provide a monetary contribution of £22,258 in lieu of an onsite affordable housing provision. However, the level of surplus is not considered to be sufficient to provide any onsite affordable housing.

5.3. Our conclusions remain valid for 6 months beyond the date of this report. If the implementation of the scheme is delayed beyond this time-frame then market conditions may have changed sufficiently for our conclusions on viability to be adjusted. Under this scenario we would strongly recommend the scheme is re-appraised.

Yours sincerely



David Newham MRICS
Director
CP Viability Ltd