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Financial Viability Assessment: Land at Foundry Close, Hurst Green

Prepared for
William & Helen Moore
The Harper Trust

September 2019

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1 Introduction

William & Helen Moore and The Harper Trust ('the Applicant') has commissioned BNP Paribas Real Estate to provide an assessment of the financial viability of their proposed residential redevelopment ('the Proposed Development') of land at Foundry Close, Hurst Green ('the Site'). We understand the land is split between two ownerships; William & Helen Moore and The Harper Trust.

The Applicant intends to submit a planning application for the redevelopment of the Site to provide 20 residential units consisting of 6 x two-bed units, 4 x three-bed units and 10 x four-bed units.

1.1 BNP Paribas Real Estate

BNP Paribas Real Estate is a leading firm of chartered surveyors, town planning and international property consultants. The practice offers an integrated service from nine offices in eight cities within the United Kingdom and over 180 offices, across 34 countries in Europe, Middle East, India and the United States of America, including 18 wholly owned and 16 alliances.

BNP Paribas Real Estate has a wide ranging client base, acting for international companies and individuals, banks and financial institutions, private companies, public sector corporations, government departments, local authorities and registered providers ('RPs').

The full range of property services includes:

- Planning and development consultancy;
- Affordable housing consultancy;
- Valuation and real estate appraisal;
- Property investment;
- Agency and Brokerage;
- Property management;
- Building and project consultancy; and
- Corporate real estate consultancy.

This report has been prepared by Amir Esmaili, BSc (Hons) MRICS and reviewed by Anthony Lee MRICS MRTPI, RICS Registered Valuer.

The Affordable Housing Consultancy of BNP Paribas Real Estate advises landowners, developers, local authorities and RPs on the provision of affordable housing.

In 2007, we were appointed by the Greater London Authority ('GLA') to review its 'Development Control Toolkit Model' (commonly referred to as the 'Three Dragons' model). This review included testing the validity of the Three Dragons' approach to appraising the value of residential and mixed use developments; reviewing the variables used in the model and advising on areas that required amendment in the re-worked toolkit and other available appraisal models and submitted our report in February 2012.

Anthony Lee was a member of the working group under the chairmanship of Sir John Harman that drafted '*Viability testing local plans: Advice for planning practitioners*'. He was also a member of the '*Developer Contributions Expert Panel*' advising MHCLG on the viability section of the 2018 Planning Practice Guidance.

In addition, we were retained by the then Homes and Communities Agency ('HCA'), now Homes England ("HE") to advise on better management of procurement of affordable housing through planning obligations.

The firm has extensive experience of advising landowners, developers, local authorities and RPs on the value of affordable housing and economically and socially sustainable residential developments.

1.2 Report structure

This report is structured as follows:

- **Section two** provides a brief description of the proposed Development;
- **Section three** describes the methodology that has been adopted;
- **Section four** outlines the inputs adopted within our appraisals;
- **Section five** sets out the results of the appraisals;
- Finally, in **Section six**, we draw conclusions from the analysis.

1.3 The Status of our advice

This report is not a valuation and should not be relied upon as such.

In accordance with PS 1.6 of the RICS Valuation – Professional Standards (2017 Edition) (the ‘Red Book’), the provisions of VPS 1 to VPS 4 are not of mandatory application and accordingly this report should not be relied upon as a Red Book valuation.

In carrying out this assessment, we have acted with objectivity, impartiality, without interference and with reference to all appropriate available sources of information.

We are not aware of any conflicts of interest in relation to this assessment.

In preparing this report, no ‘performance-related’ or ‘contingent’ fees have been agreed.

This report is addressed to the Applicant only and should not be reproduced without our prior consent.

2 Background and Description of the Development

2.1 The Site

The Site is located in Hurst Green Parish within Rother District, East Sussex. Specifically, the Site is located to the rear of Foundry Close which is accessed via London Road with Etchingam Station (National Rail) approximately 1.7 miles to the east of the Site.

The Site falls within the High Weald Area of Outstanding Natural Beauty and thus presents additional development considerations that will need to be accounted for.

The Site lies on the east side of London Road, north of the main village centre. The Site measures approximately 0.80 hectares and is currently occupied by greenland. Ernest Doe Power farming supplies, a 2-storey industrial unit, sits to the west of the Site and there are a number of residential properties located within the vicinity ranging from 2-3 storeys in height. We understand the Site is held freehold by the Applicant's, ownership outlined above, and we understand there is no current planning consent for redeveloping the site.

2.2 The Proposed Development

We understand there is a historic planning application which was refused, and subsequently appealed, the details of which are as follows;

"Residential development of site to provide 60 dwellings (RR/2016/1577/P)".

We understand the appeal was dismissed on 24 October 2017.

The Applicant is seeking planning permission for the redevelopment of the Site to provide 20 residential units consisting of 6 x two-bed units, 4 x three-bed units and 10 x four-bed units.

We have been provided with the following accommodation schedule the details of which we set out below in Table 2.2.1.

Table 2.2.1 Proposed Unit Mix

Unit Type	Size (sq/ft)	Bedrooms	No. Units
A	1,087	4	7
B	1,055	3	4
C	1,216	4	3
D1	861	2	1
D2	840	2	1
E	872	2	2
F	818	2	2
Total	20,559	-	20

3 Methodology

We have used Argus Developer ('Argus') to appraise the development proposals. Argus is a commercially available development appraisal package in widespread use throughout the industry. It has been accepted by a number of local planning authorities for the purpose of viability assessments and has also been accepted at planning appeals. Banks also consider Argus to be a reliable tool for secured lending valuation. Further details can be accessed at www.argussoftware.com.

Argus is essentially a cash-flow model. Such models all work on a similar basis:

- Firstly, the value of the completed development is assessed.
- Secondly, the development costs are calculated, including either the profit margin required or land costs. In our appraisals we include profit as a development cost.

The difference between the total development value and total costs equates to the residual land value ('RLV'). The model is normally set up to run over a development period from the date of the commencement of the project until the project completion, when the development has been constructed and is occupied.

The cash-flow approach allows the finance charges to be accurately calculated over the development period. This approach can accommodate more complex arrangements where a number of different uses are provided or development is phased.

In order to assess whether a development scheme can be regarded as being economically viable it is necessary to compare the RLV that is produced with a benchmark land value. If the Development generates a RLV that is higher than the benchmark it can be regarded as being economically viable and therefore capable of providing additional affordable housing and Section 106 payments. However, if the Development generates a RLV that is lower than the benchmark it should be deemed economically unviable and the quantum of affordable housing and Section 106 payments may need to be adjusted until viability is achieved.

National Planning Practice Guidance ('NPPG') paragraph 013 (reference ID 10-013-20190509) indicates that benchmark land values 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. The premium should provide a reasonable incentive, in comparison with other options available, for the landowner to sell land for development while allowing a sufficient contribution to comply with policy requirements"*.

4 Assumptions

This section of the report sets out the general principles and assumptions which have been used to undertake a development appraisal of the scheme.

4.1 Economic and Housing Market Commentary

The UK's impending departure from the European Union continues to be a major source of uncertainty within British politics. A deal is yet to be agreed. Theresa May lost the 'meaningful vote' on her Exit plan and narrowly survived the subsequent no-confidence vote. She is calling for cross party consensus but there remains very little agreement on the structure of the UK's future relationship with the EU either within her party or across parties. The result of this is that considerable political uncertainty remains and it is extremely difficult to predict when this will change. This is feeding through into a very cautious and unknown economic outlook from most commentators.

The National Institute for Economic and Social Research¹ estimates that the UK economy grew by 0.3% over the course of Q4 2018, which was lower than the growth rate achieved in Q3 (0.6%). This is consistent with the HM Treasury central forecast that over the course of 2018 the UK economy grew by c.1.3%. The forecast for growth during 2018 gradually dropped throughout 2018, although not considerably, and finished the year broadly as expected. For 2019 the forecast has remained largely unchanged, ranging from 0.9% to 2.2% with an average forecast of 1.5%.

On the other hand, the British Chamber of Commerce (BCC)² are predicting a lower growth of 1.3% for 2019. For 2020 they have downgraded their forecast from 1.6% to 1.5%. The BCC claims a disorderly departure from the EU is the key to the UK's economic outlook as it would likely weaken the UK's short-term growth and productivity.

The ICAEW measures business confidence on a scale of -100 to +100 (+100 being extremely confident, 0 being neutral, -100 being extremely negative).³ In Q3 2018 the UK scored -2. Q4 2018 has seen a reduction in confidence and the UK now scores -12.3. This is the lowest that business confidence has been in the UK since the financial crash.

From a regional perspective, in Q3 2018 many parts of the country such as the West Midlands, Scotland and the East of England reported positive business confidence. However, in Q4 2018 all regions across the UK have reported negative confidence. Wales is the most confident region with a score of -6. London has a business confidence of -9.1. Despite being negative this is above the UK average of -12.3. The ICAEW claim the decline in confidence seen in Q4 2018 set in immediately after the PM unveiled the draft UK-EU agreement.

The latest figures from the Office for National Statistics ('ONS') show that inflation (CPIH) in November 2018 was at 2.2%. This is unchanged from the previous month but lower than the inflation rate a year ago (2.8%). The cause for this drop off over the past 12 months has been a reduction in the cost of petrol and recreational goods and services.

The Bank of England ('BoE') have maintained the 0.75% interest rate. The BoE are still planning to reach an interest rate of 2.0% by 2021. What happens to the economy in the coming months, particularly post 29 March, may have an influence on whether this target needs to be revised.

In December 2018 the FTSE 100 was at the lowest it has been since 2016. It has since had a slight uptick but remains low relative to the past year. Relative to the past five years it remains strong however. In the year 2015 the average value of the Pound to the Euro was 1.38, the equivalent figure over the course of 2018 was 1.13. This shows that the Pound has fallen by 18% relative to the Euro. As of the start of January 2019 the exchange rate is 1.11 and is the third lowest it has been over the past twelve months.

¹ NIESR, GDP growth tracker, 2018

² British Chamber of Commerce, BCC forecast: Uncertainty constraining UK economic growth, 2018

³ ICAEW, business confidence monitor, 2018

According to the Nationwide House Price Index (NWHPI), UK property prices grew 1.3% over the course of 2018. Year on year growth over the same period shows that on a regional basis the best performer has been Northern Ireland (5.8%) followed by the East Midlands (4.0%) and Wales (3.9%). As seen throughout 2018, London, which historically has always had the strongest growth across the UK, had one of the lowest growth rates (-0.9%). The only other region to register a negative growth at the end of year was the Outer Met (-1.4%).

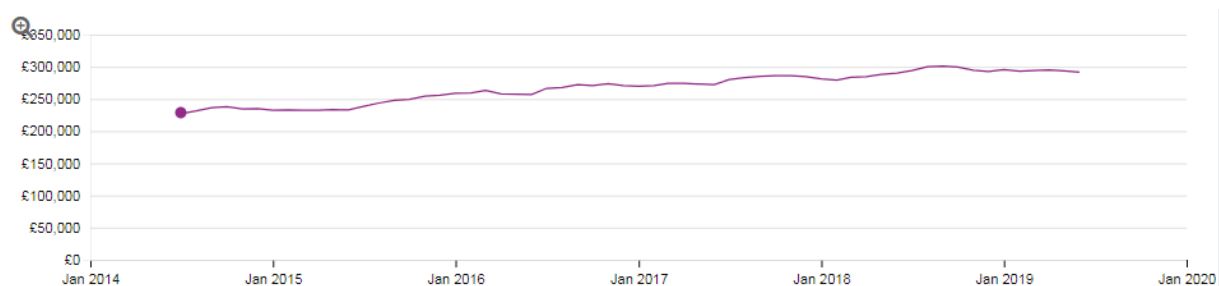
Nationally, house prices are now 16.5% above their pre-crisis peak and London prices are 53.7% above their pre-crisis peak. In Q4 2018, three regions, Northern Ireland (-38.6%), the North (-6.0%) and Scotland (-2.9%), still remained below their pre-crisis peak.

Substantial economic and political uncertainty remains both nationally and globally and it does not look likely that this will change any time soon. The likely outcome of the UK's ongoing negotiations with the EU remains extremely uncertain. The route Britain takes will have significant implications for the UK and the rest of Europe. The fundamentals of the UK economy remain broadly positive, but sentiment remains cautious with constant negative media resulting in indecision within many markets.

Appropriate pricing and the continued attractiveness of Sterling will continue to be key factors affecting market activity levels in the higher price sectors. There is the possibility of further price decreases in 2019 as globally and domestically the economy and political environment remain volatile. Beyond 2019 it is extremely difficult to forecast this market with any certainty, but we would expect some bounce back once more stability has returned.

Over the past 12 months property prices in the Rother District have fallen by 4.5%. Figure 4.1 below shows the average property prices in Rother over the last five years.

Figure 4.1 Average Property Price Rother District: July 2014 – July 2019



4.2 Gross Development Value ('GDV')

4.2.1 Residential Sales Values

As the Site is located within a rural area there is difficulty identifying newly built comparable evidence. As such, we have had regard to recent sales transactions of second hand stock within the Hurst Green area to determine the values achievable at the proposed development.

We summarise below the range of values for each unit type within Hurst Green.

Table 4.2.1 Comparable Sales Evidence

Unit	Min. Price (£)	Max. Price (£)	Size (sq/ft)	Avg. £PSF
Two Bedroom	£153,000	£270,000	506 – 883	£309
Three Bedroom	£220,000	£375,000	786 – 1,195	£316
Four Bedroom	£345,000	£411,000	1,163 – 1,453	£295

Having considered the above sales evidence, we have prepared our own unit pricing at the subject site taking into consideration factors such as location, specification, access to public transport and amenities.

We summarise in Table 4.2.2 our average proposed sales values.

Table 4.2.2 BNPPRE Average Private Values

Unit Type	Average Anticipated Sales Value (£)	Average £PSF
A	£380,000	£350
B	£360,000	£341
C	£410,000	£337
D1	£305,000	£354
D2	£300,000	£357
E	£310,000	£356
F	£295,000	£361

This generates a total capital value of £6,850,000, equating to an overall average of £348 per sq/ft.

4.2.2 Ground Rents

In October 2018 Ministry for Housing, Communities and Local Government issued a second consultation on 'Implementing reforms to the leasehold system in England' indicating the government's preference for a £10 per annum ground rent.

The consultation indicates that should proposals be taken forward in 2019, "*any legislation would [be] unlikely to complete its passage until mid-2020 at the earliest*". However, as the development is proposing individual homes, we assume these to be sold on a freehold basis, and as such, ground rents would not be applicable.

4.3 Development Costs

4.3.1 Construction Costs

We have not been provided with a cost plan, therefore, we have relied upon costs obtained through the Build Cost Information Services (BCIS). We have adopted the "5 Year Upper Quartiles" cost for "Estate Housing Terraced" up to 2-storeys which equates to £143 per sq/ft.

As the BCIS does not account for any external works or contingencies, we have made the following allowances on top of the base build cost.

Table 4.3.1 BNPPRE Additional Construction Costs

Construction Type	Unit
External, Services, Utilities	10%
Contingency (Developer)	5%
Contingency (Construction)	5%

In addition to the above costs we have also made an allowance for Professional Fees of 10% in accordance with our experience of schemes of this nature.

Furthermore, as the Site is located within the High Weald Area of Outstanding Natural Beauty, we have been advised of additional abnormal costs that would need to be considered to accommodate the onsite ecological issues.

We have been made aware of the following onsite requirements from the Applicant's Landscape Architect;

Coppice Woodland

Coppice woodland area (c.0.14ha) to comprise, scrub and tree planting including hazel (Corylus avellana), guelder rose (Viburnum opulus), holly (Ilex aquifolium), dogwood (Cornus sanguinea), spindle (Euonymus europaeus) and dog rose (Rosa canina).

6 hazel dormouse nest boxes and 5 'dug-in' log piles to be installed within compensatory habitat area. Compensatory areas to be managed under a 15-year rotational coppice regime.

Hedgerows

Approximately 0.07ha of new native species hedgerow plantings throughout the site.

An appropriate hedgerow species mix could include hawthorn (50%), field maple (Acer campestre) (30%), hornbeam (Carpinus betulus) (10%), guelder rose (3%), dogwood (Cornus sanguinea) (3%), spindle (Euonymus europaea) (2%) and dog rose (Rosa canina) (2%).

Where landscape and visual amenity constraints do not apply, the new hedgerows will be allowed to grow to at least 3m high and 2m wide and will not be reduced below these dimensions during subsequent management of the site. Hedgerows will be managed to the recommended dimensions listed above.

We summarise below the costs associated with remediating the ecological requirements;

Table 4.3.2 Abnormal Ecological Costs

Element	Unit (per sq/m)	Unit Area (sq/m)	Total Cost
Coppice Woodland	£10	1,400	£14,000
Hedgerows	£5	700	£3,500
Total	-	-	£17,500

4.3.2 Interest

Where development finance is available (which is only in a select number of situations) lenders are currently charging up to 5% above LIBOR with minimum rates of at least 6.5%. High arrangement (1-3%), monitoring (2-5%) and exit fees (1%) are also charged. These onerous lending terms have emerged due to the perceived risk of residential development in the current market.

We have adopted an interest rate of 7%, with no additional allowance for fees. It should be noted that although a bank would not provide 100% of the funding required for the Development it is conventional to assume finance on all costs in order to reflect the opportunity cost (or in some cases the actual cost) of committing equity to the project.

4.3.3 Developer's Profit

We have applied a Developer's Profit of 20% of the private housing Gross Development Value.

4.3.4 Marketing and disposal

We have adopted the following marketing and disposal costs for the residential accommodation:

- Private residential marketing at 1.5% of GDV;
- Private residential agent fees at 1.5% of GDV; and
- Residential Legal fees at £1,000 per unit;

4.3.5 Acquisition costs

Our appraisals incorporate standard acquisition costs, shown below as a percentage of the residual land value:

- Stamp Duty Land Tax: 5%;
- Acquisition agent's fee: 1%; and
- Acquisition legal fees: 0.5%.

4.3.6 CIL Section 106 Payment

The Applicant has not provided us with any formal CIL payment information, therefore, we have conducted our own assessment on the CIL payments.

We summarise below in Table 4.3.6 details of the CIL payments adopted within our appraisal;

Table 4.3.6 CIL Charging Rates

Element	Cost (£ per sq/ft)	GIA (sq/ft)	Total Cost
CIL (Indexed from July '16) Residential	£22	19,569	£434,520

The adopted CIL costs generate a total contribution of £434,520 which we have adopted within our appraisal.

At present, we have not been made aware of any S106 contributions required, therefore, upon receipt of further information from either the Applicant or the Council we reserve the right to revisit this cost at a later date.

4.3.7 Project Timetable

We have assumed that the development will commence after a three-month pre construction period in order to place the necessary contracts and have assumed a construction period of 20 months.

With respect to the sales of the residential accommodation we have assumed that sales will commence within month 10 of the construction period. This is due to the fact that the residential units will be completed in blocks and will be capable of occupation once completed. This results in a total sales period of 15 months.

5 Appraisal Results

In this section, we consider the outputs of the appraisals and the implications for the viable level of affordable housing within the Proposed Development.

5.1 Benchmark Land Value

In order to assess the economic viability of the Proposed Development it is necessary to compare the residual land value it generates with an appropriate benchmark land value.

The Site currently consists of greenland extending to approximately 0.805 hectares.

The Rother Local Plan Viability Assessment (October 2018) states that for the purposes of viability the following values should be adopted;

Table 5.1.1 BLV For Greenfield and Brownfield Non-Residential Land (Rother Local Plan p.39)

<i>Location</i>	<i>Existing Land Use</i>	<i>EUV</i>	<i>Premium</i>	<i>BLV (i.e. EUV+) Gross</i>
<i>Rural West</i>	<i>Agricultural / Greenfield</i>	<i>£25,000</i>	<i>20</i>	<i>£500,000</i>

5.2 Appraisal Results

We summarise below the details of our appraisal results.

Table 5.2.1 BNPPRE Appraisal Results

Proposed Scheme Residual Land Value	Benchmark Land Value	Surplus / Deficit
c. £0.67m	£0.50m	c. £0.17m

A copy of our development appraisal is attached as **Appendix 1**.

6 Conclusions

Our assessment of the proposed scheme with 100% private housing demonstrates that the scheme generates a surplus of c. £0.17m when benchmarked against a site value of £0.50m.

In accordance with adopted practice we have approached our viability assessment on a PPG compliant basis using standardised inputs which does not reflect the Applicant's specific circumstances.

Given that the surplus would generate a low quantum of affordable housing we do not consider this as being attractive to a housing association to take on a low quantity of units. In contrast, we consider a payment in lieu for an offsite contribution towards affordable housing of c. £0.17m as being more appropriate.

Appendix 1 – Proposed Scheme Appraisal Summary

BNP Paribas Real Estate

Development Appraisal

Land at Foundry Close

100% Private Unit Sales

Hurst Green
Rother
East Sussex

Report Date: 16 September 2019

**Land at Foundry Close
100% Private Unit Sales**

Summary Appraisal for Phase 1

Currency in £

REVENUE					
Sales Valuation	Units	ft²	Rate ft²	Unit Price	Gross Sales
Private Units	20	20,559	347.54	357,250	7,145,000
NET REALISATION				7,145,000	
OUTLAY					
ACQUISITION COSTS					
Residualised Price				672,520	
Stamp Duty		5.00%		33,626	
Agent Fee		1.00%		6,725	
Legal Fee		0.50%		3,363	
					716,234
CONSTRUCTION COSTS					
Construction	ft²	Rate ft²	Cost		
Private Units	20,559 ft²	143.00 pf²	2,939,937	2,939,937	
Contractors Contingency		5.00%	169,046		
Developers Contingency		5.00%	169,046		
Ecological Conservation (Dormice)			17,500		
CIL			434,520		
					790,113
Other Construction					
Externals / Services / Utilities		15.00%	440,991		
					440,991
PROFESSIONAL FEES					
Professional Fees		10.00%	371,902		
					371,902
MARKETING & LETTING					
Marketing		1.50%	107,175		
					107,175
DISPOSAL FEES					
Sales Agent Fee		1.50%	107,175		
Sales Legal Fee	20 un	1,000.00 /un	20,000		
					127,175
Additional Costs					
Profit on GDV (Private)		20.00%	1,429,000		
					1,429,000
FINANCE					
Debit Rate 7.000% Credit Rate 0.000% (Nominal)					
Land				96,959	
Construction				123,229	
Other				2,286	
Total Finance Cost					222,473
TOTAL COSTS				7,145,000	
PROFIT					0
Performance Measures					
Profit on Cost%		0.00%			
Profit on GDV%		0.00%			
Profit on NDV%		0.00%			
IRR		6.48%			
Profit Erosion (finance rate 7.000%)		N/A			