DRAFT VIABILITY REPORT

For the Project

At

CRESSINGHAM GARDENS

Prepared On Behalf Of

LONDON BOROUGH OF LAMBETH

Date: 3rd July 2015
Reference: *14/124 Version 7*

Version Control

Version	Date	Author	Page No(s)	Comments
V1	2 June 2015	MG	18	Draft for approval
V2	4 June 2015	MG	21	Draft for approval
V3	8 June 2015	MG	20	Draft for approval
V4	15 June 2015	MG	21	Draft for approval
V5	23 June 2015	MG	23	Draft for approval
V6	2 July 2015	MG	21	Draft for approval
V7	3 July 2015	MG	21	Draft for approval

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1. INTRODUCTION

The London Borough of Lambeth has committed to a programme of estate regeneration within the Borough to bring about long-term improvements to its housing stock and the quality of living for its residents.

To bring about this change the Council has been looking at viable options to refurbish and extend the lifespan of existing stock to provide good quality housing to meet the needs of residents. It has also been looking at areas within the Borough with development potential, including its own estates, to bring forward additional housing in the Borough to help meet the growing number of households wishing to live there.

As part of this programme, the Council has identified the housing stock on the Cressingham Estate ("the site") as being in need of improvement and with the potential for delivering an up-lift in the number of homes.

Airey Miller Partnership has been commissioned to complete financial analysis of the preliminary options being considered by the Council and to report on the relative merits in financial terms of the options being explored.

The scenarios tested demonstrate how by flexing some of the key priorities underpinning regeneration on the site, the capital cost, funding requirements and level of cross-subsidy generated interlinks to bring about different outcomes and risk profiles for the Council.

The purpose of this report is therefore to provide an overview of the financial viability of the site summarising work to date and setting out a series of scenarios for consideration by the Council.

An initial viability has been carried out on two options to show a base option based on the Council's aspirations in terms of the ability to cross subsidise the anticipated refurbishment costs, provide the requisite level of affordable housing provision and deliver any new build housing.

This base option has demonstrated that the two development options are viable, but do require modest adjustments to the Councils principle objectives and aspirations. Consequently, further scenario testing has been undertaken to understand the effects of changes to these requirements and to present the Council with a number of options to allow the Council to make informed decisions on how and where there is flexibility in the proposed development strategy. These options are presented in Section 4 of this report.

1.1 Delivery from the proposed options

The Council is considering two development options. These options have been produced as part of the feasibility and massing exercise completed by Karthaus Design and summarised in the Cressingham Gardens Summary Report dated March 2015:

- ***Option 4 Partial Redevelopment with Refurbishment***
  This option sees the demolition of Crosby, Longford, Scarlette, Papworth and Chandler. In total:
  121 homes demolished
  93 tenants
  28 leaseholders/ freeholders

  Replaced with 193 new homes and Refurbishment of retained stock

- ***Option 5 Comprehensive Redevelopment***
  This sees the entire estate demolished. In total:
  306 homes demolished
  212 tenants
  94 leaseholders/ freeholders

  Replaced with 464 new homes

1.2 Delivery Aspirations

Under both base options, it is been assumed that the regeneration proposals will re-provide the existing stock as far as practicable (re-providing the equivalent unit size mix as currently exists).

It is assumed under the refurbishment option (Option 4) that the regeneration project for the redeveloped part of the estate will provide the funding for refurbishment. This represents 2/3 of the £8m indicative cost of work. This is included in the financial appraisal as an additional cost during the development works. A proportion of this is assumed to be subsequently recouped from leaseholders.

A Right to Buy capital allocation of £1.68m is assumed for enabling and acquisitions. A Right to Buy capital input is also assumed against 30% of the net gain affordable housing construction costs.

Airey Miller is advised by the Council that it has set out clear minimum objectives for regeneration. These are:

- To re-provide homes for all those wishing to remain on an estate. For the purposes of the estate regeneration this means:
  - Re-providing existing tenants with an equivalent new home
  - Re-providing 80% of leaseholders with an equivalent new home
- To fix the rent for existing tenants to the equivalent of a social or target rent (i.e. homes at council rent levels)
- As a minimum, to ensure that the net gain additional new homes meet Council policy:
  - Planning Policy requires a minimum of 40% affordable homes
  - Tenancy Strategy requires that 1 and 2 bedroom properties be let at maximum of LHA rates and family homes (3 bedrooms and larger) be let at target rents

The Council has also declared its aspirations as set out below:

<u>Tenure of net gain homes</u>
- 60% affordable
  - made up from 100% Council Rent
- 40% private rent

<u>Unit Size Mix of net gain homes</u>
- 1 Bed – 15%
- 2 Bed – 50%
- 3 Bed – 25%
- 4 Bed – 10%

<u>Rents</u>
- Net gain affordable homes to be provided at council rent levels (otherwise known as Target Rent)

1.3 Programme and Decanting

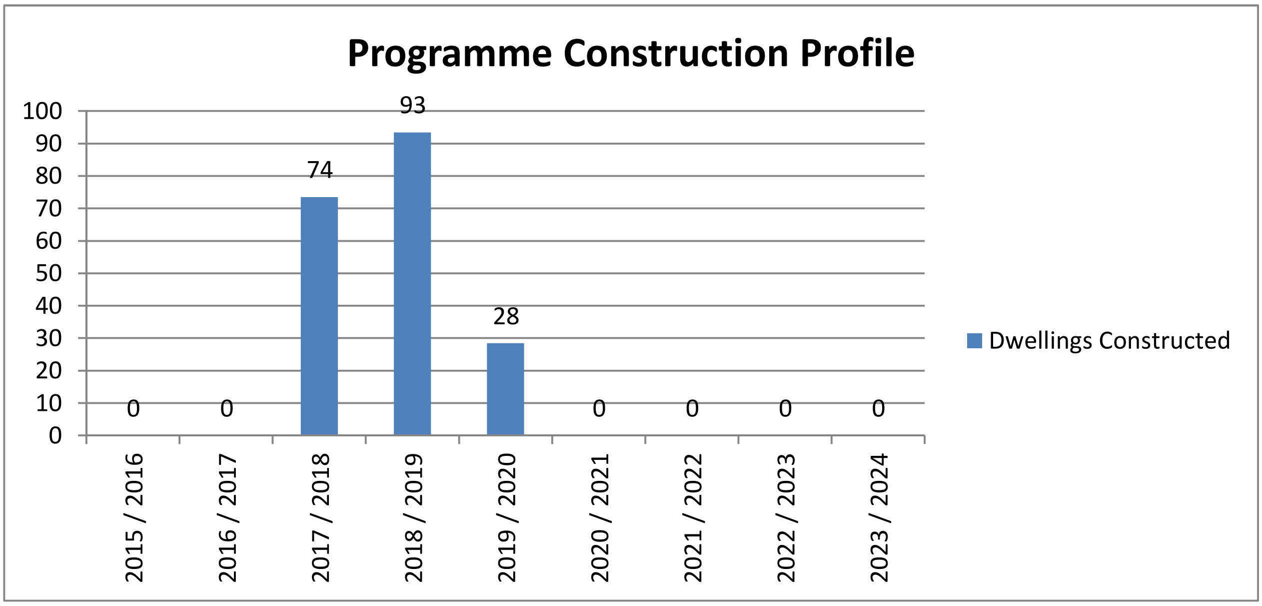
The programme for the development options is based on a sequenced decant strategy that is aligned to the construction programme. It is acknowledged that the Council may deviate from this timeline, securing properties as and when they become available.

Broadly, development is proposed to take place in a continuous phase with site preparation concluding in the first quarter of 2017. Construction and refurbishment work will commence in the second quarter 2017 with work taking approximately 139 and 244 weeks respectively for Option 4 and Option 5.

The delivery profile is illustrated below for the base options:

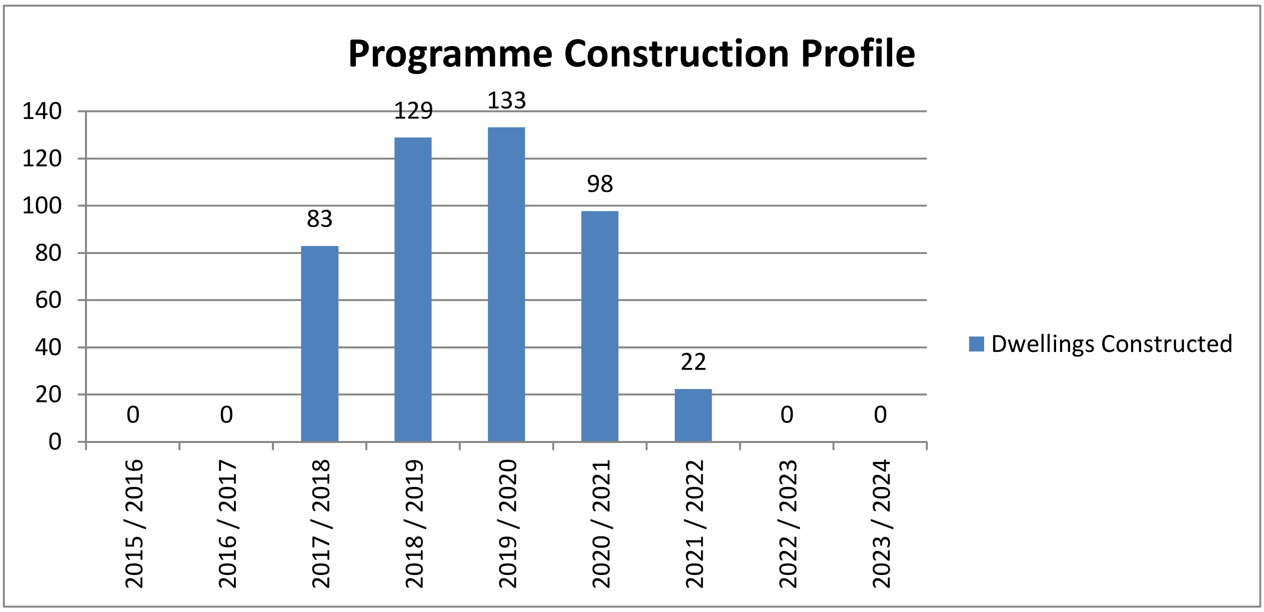
Option 4

Delivery Profile



Option 5

Delivery Profile



2. FINANCIAL VIABILITY ANALYSIS

The purpose of this financial viability analysis is to establish whether the options proposed to bring about estate regeneration at Cressingham Gardens are viable and deliverable, providing the Council with an acceptable risk profile and a positive net present value ("NPV").

NPV is a measure of how profitable a future cashflow is by comparing the value of a pound today to the value of that pound at a future point, taking inflation into account. If the NPV of a prospective project is positive, the project stands to provide an increased return on investment and would be considered acceptable. However, if NPV is negative, the project probably should be rejected because the cost of implementing will not be recovered in the future.

In terms of the financial structure, it is recognised that the Council is still considering a number of different finance approaches. For the purpose of this analysis, the financial appraisal is operating a tiered funding structure. In brief, this approach enables:

- Development finance cost to be rolled-up
- Re-finance after Practical Completion. Ability to borrow more than development cost if there is sufficient headroom within LTV limit of asset.
- Tier One (Senior debt) to be re-paid as a priority before Tier Two Finance (Subordinated debt)
- Income commences upon occupation under PRS scenario. Private sales enable income to be realised earlier through off-plan sales and earlier hand-over during construction.

3. BASE OPTION

A base option has been considered for each development proposal. The base option takes account of the Council's objectives and aspirations detailed earlier in this report and determines the extent to which these ambitions can be achieved.

The base option delivers the following outcomes:

Option 4

No. of dwellings proposed fits Karthaus design (193)	Achieved
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	Achieved
Net gain homes meet Planning Policy (40% affordable housing)	Achieved
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Achieved
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved
Net Gain Private delivered as Private Rent	Flex – 60% private sale
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£798,808
Finance Cost	£66,364,183
Breakeven achieved in	Sept-73

Option 5

No. of dwellings proposed fits Karthaus design (464)	Achieved
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	Achieved
Net gain homes meet Planning Policy (40% affordable housing)	Achieved
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Achieved
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved
Net Gain Private delivered as Private Rent	Flex – 60% private sale
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£13,013,539
Finance Cost	£99,700,039
Breakeven achieved in	Dec-59

4. SCENARIO TESTING

It is recognised that it is preferable for the Council to achieve as many of its ambitions as possible, within the most acceptable risk profile.

To assess and provide visibility of some of the potential options available to the Council to secure improvements, Airey Miller Partnership has tested a number of viability scenarios. Using the base option as the starting point, sequential alterations have been made to the principle assumptions to capture and articulate the potential scope for enhancement.

In conducting these viability scenarios, three principle assumptions have been explored. These are dwelling density, tenure of private net gain dwellings, and level of affordable rents.

4.1 Outcomes of Scenario Testing

The outputs are summarised over the following pages.

<u>Option 4 – Partial Redevelopment with Refurbishment</u>

<u>Base Option</u>
Based on 193 dwellings and a refurbishment cost of £5.3m a viable scheme is achievable. The replaced affordable properties are re-provided at Target Rent.

This relies on a 40/60 affordable to private tenure split on the net gain element. The affordable element is provided in accordance with the Council's Tenancy Strategy and the private net gain element is completely provided (100%) as private sale.

Option 4.1

To enable the Council to deliver an element of private rent instead of private sale, the development would need to deliver 210 dwellings. By removing the early income receipt associated with private sales increases the cost of borrowing and extends the breakeven period.

No. of dwellings proposed fits Karthaus design (193)	Flex – 210 dwellings
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	Achieved
Net gain homes meet Planning Policy (40% affordable housing)	Achieved
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Achieved
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved
Net Gain Private delivered as Private Rent	Achieved
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£399,882
Finance Cost	£226,008,281
Breakeven achieved in	Sept-75

Option 4.2

To enable the Council to deliver a scheme aligned to the proposed number of dwellings and an element of private rent instead of private sale, the development would need to deliver 1 and 2 bed net gain affordable properties at 80% of private rent values (otherwise known as discount rent). The 3 bed+ properties are at Council Rent levels.

No. of dwellings proposed fits Karthaus design (193)	Achieved
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	Achieved
Net gain homes meet Planning Policy (40% affordable housing)	Achieved
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Flex – 40% Planning Policy at 80% OMRs (Discount rent)
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved
Net Gain Private delivered as Private Rent	Flex – 9% private rent and 51% private sale
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£2,217,691
Finance Cost	£70,863,815
Breakeven achieved in	Sept-70

Option 4.3

With a scheme providing 210 dwellings, it could be possible to deliver 60% affordable housing in the net gain element. It would enable the initial 40% net gain affordable element to have rents at Tenancy Strategy levels, with the additional 20% net gain affordable having rents at 80% of OMR's (or otherwise known as discount rents). The private element would be delivered as 20% private rent and 80% private sale.

No. of dwellings proposed fits Karthaus design (193)	Flex – 210 dwellings
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	Achieved
Net gain homes meet Planning Policy (40% affordable housing)	Flex – 60% affordable delivered on net gain
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Achieved – 40% Planning Policy at Tenancy Strategy with additional 20% at 80% OMR's
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved – 40% Planning Policy at Tenancy Strategy with additional 20% at 80% OMR's
Net Gain Private delivered as Private Rent	Flex – 8% as private rent and 32% private sale
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£415,854
Finance Cost	£118,450,663
Breakeven achieved in	Jun-75

Option 5 – Comprehensive Redevelopment

Base Option

Based on 464 dwellings a viable scheme is achievable.

The net gain element of the scheme delivers a 40 / 60% split between affordable and private tenures. The affordable housing delivery is in accordance with the Council's Tenancy Strategy. The private element relies on 100% private sale.

Option 5.1

To enable the Council to deliver an element of private rent instead of private sale, the development would need to deliver 522 dwellings. By removing the early income receipt associated with private sales increases the cost of borrowing and extends the breakeven period.

No. of dwellings proposed fits Karthaus design (464)	Flex – 522 dwellings
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	Achieved
Net gain homes meet Planning Policy (40% affordable housing)	Achieved
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Achieved
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved
Net Gain Private delivered as Private Rent	Achieved
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£1,868,312
Finance Cost	£542,211,278
Breakeven achieved in	Jun-75

Option 5.2

The Council is able to deliver a scheme aligned to the proposed number of dwellings and an element of private rent instead of private sale. It would also be able to deliver net gain affordable properties at Council Rent levels.

No. of dwellings proposed fits Karthaus design (464)	Achieved
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	Achieved
Net gain homes meet Planning Policy (40% affordable housing)	Achieved
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Achieved
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved
Net Gain Private delivered as Private Rent	Flex – 24% as private rent and 36% private sale
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£800,358
Finance Cost	£275,386,901
Breakeven achieved in	Jun-75

Option 5.3

With a scheme providing 522 dwellings, it could be possible to deliver 60% affordable housing in the net gain element. It would enable the initial 40% net gain affordable element to have rents at Tenancy Strategy levels, with the additional 20% net gain affordable having rents at 80% of OMR's (or otherwise known as discount rents). The private element delivers 70% private rent and 30% as private sale.

No. of dwellings proposed fits Karthaus design (464)	Flex – 522 dwellings
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	Achieved
Net gain homes meet Planning Policy (40% affordable housing)	Flex – 60% affordable delivered on net gain
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Achieved – 40% Planning Policy at Tenancy Strategy with additional 20% at 80% OMR's
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved – 40% Planning Policy at Tenancy Strategy with additional 20% at 80% OMR's
Net Gain Private delivered as Private Rent	Flex – 28% as private rent and 12% private sale
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£10,651,265
Finance Cost	£358,487,814
Breakeven achieved in	Mar-71

Option 5.4

It is possible to deliver all the private net gain properties as private rent and deliver 60% affordable housing by delivering the planning policy 1 and 2 bed net gain affordable properties at 70% of private rents and the additional 20% affordable housing at 80% of private rents.

No. of dwellings proposed fits Karthaus design (464)	Flex – 522 dwellings
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	Achieved
Net gain homes meet Planning Policy (40% affordable housing)	Flex – 60% affordable delivered on net gain
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Achieved – 40% Planning Policy at 70% OMR's with additional 20% at 80% OMR's
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved – 40% Planning Policy at Tenancy Strategy with additional 20% at 80% OMR's
Net Gain Private delivered as Private Rent	Achieved
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£3,737,786
Finance Cost	£489,138,416
Breakeven achieved in	Sep-74

Option 5.5

It is possible to deliver the improve affordability of the affordable housing rents but this deliver 70% of the net gain private properties as private rent. The 1 and 2 bed net gain affordable properties can be delivered at 93% of LHA caps with the 3 bed properties at Council Rent.

No. of dwellings proposed fits Karthaus design (464)	Achieved
Housing Size Mix	Achieved
Re-provide existing homes at Target Rent	Achieved
Fund Refurbishment Cost	N/A
Net gain homes meet Planning Policy (40% affordable housing)	Flex – 50% affordable delivered on net gain
Net gain 1 and 2 bed affordable homes meet Tenancy Strategy	Achieved – 40% Planning Policy at Tenancy Strategy with additional 10% at 80% OMR's
Net gain 3 bed (or more) affordable homes meet Tenancy Strategy	Achieved – 40% Planning Policy at Tenancy Strategy with additional 10% at 80% OMR's
Net Gain Private delivered as Private Rent	Flex –5% as private rent 45% private sale
Nil pump priming investment from LBL	Achieved
Finance at Council Rate	Achieved
NPV	£7,461,451
Finance Cost	£173,521,736
Breakeven achieved in	Sept-68

5. SUMMARY

Through our financial analysis of the two development options, it is evident that the Cressingham Gardens Estate is viable for regeneration.

The base options presented recognise the key objectives of delivering within the principle policy requirements of the Council.

The scenario testing then further demonstrates the scope for further refinement moving forward. Within the scenario testing reported here, it is evident that there is sufficient scope to flex the base option to achieve more of the Council's aspirations or to achieve a greater NPV.

Notes and Exclusions

- Numerous input data remains to be refined by the client and other advisors, the current model output is therefore not representative of the final scheme position.
- Indicated finance costs will not be accurate where the scheme does not reach a positive position.
- The finance structure is indicative and will need to be agreed with the eventual funder.
- This model has been prepared at an early stage in the project development based on limited information; the results of the model may therefore change in line with scheme / financial development. A further iteration of the model will be undertaken in due course.
- The gross and net rent cashflow is intended to be indicative only. A full business plan including major repair and replacement should be produced to inform cashflow.
- Airey Miller accepts no liability for the accuracy of input data other than that provided by Airey Miller Partnership. In particular, no liability is accepted in respect of values or income or operational/management costs. At present, the model uses affordable values as advised by the Council and those set out in the Local Housing Allowance for Inner South East London, June 2015. The Open Market Sales and Rental Values reported to the Council are provided by Lambert Smith Hampton and Hamptons International. These will need to be checked for a more location specific value weightings going forward.
- Airey Miller Partnership accept no liability for user changes to the model, any proposed changes should be referred to Airey Miller Partnership for checking.
- Airey Miller Partnership has produced its own Order of Costs to inform the cost assumptions. It is intended that these OoC’s provide a consistent and up to date base date. The detail is based on the previous design work and it is assumed that the design will work around the existing infrastructure layout. If there is a need to re-route services etc. then this will incur additional cost.
- The NPV figures reported are illustrative only. Cost and values will fluctuate during the development period and it is recommended that the financial position is constantly monitored to ensure financial performance is maintained.
- There may be minor discrepancies between the figures presented owing to rounding in the calculations within the financial model.