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Ms. Samantha Moreira
Directorate of Regeneration, Enterprise and Skills,
Royal Borough of Greenwich
The Woolwich Centre,
35 Wellington Street,
London SE18 6HQ

cc. Mike Hows; Andrew Parker

17-8-15

Dear Ms Moreira,

Further to the instructions of the Royal Borough of Greenwich to consider the financial viability submission regarding the Greenwich Peninsula 2015 Masterplan, we are pleased to submit our professional views as requested. As you know, we have been much involved with this Project since 2002, and remain keen to see its completion. Nevertheless, as you know, the proposals have been difficult to implement, so we are required to advise the Council again, following extensive discussions with applicants and their advisors (BNP Paribas), as to the current Viability issues.

1. Development Appraisals

While you are familiar with the Appraisal methodology, a brief resume can be helpful. Development Appraisal models are in essence simple and can be summarised via the following equation;

Completed Development Value

Minus

Total Construction Costs

Minus

Developers Profit

=

Residual Land Value

Residual Value – what the landowner receives – will normally be the critical variable. If a proposal generates sufficient positive land value, crucial in normal cases, it will

be implemented. If not, unless there are alternative funding sources to bridge the 'gap', the proposal will not go ahead.

The problems with Development Appraisals all stem from the requirement to identify the key variables – values, costs etc.- with some degree of accuracy in advance of implementation. Even on the basis of the standard convention, namely that current values and costs are adopted (not values and costs on completion), this can be very difficult.

Problems with key variables can be summarised as follows:

- Values attached to Completed Development Value are largely dependent on comparable evidence which requires sufficient new development in the locality of a similar size and type, to provide a realistic value base. This is a particular issue in the current market circumstances.

- Development costs are subject to extensive national and local monitoring and can be reasonably accurately assessed in 'normal' circumstances. Increasingly however, with restrictions on greenfield developments and a greater emphasis on brownfield sites, 'exceptional' costs such as decontamination are becoming more common. Such costs can be very difficult to anticipate before detailed site surveys.

- Development value and costs will also be significantly affected by assumptions about the nature and type of affordable housing provision and other Planning Obligations / CIL and on major projects, assumptions about development phasing and infrastructure triggers.

- While Developer's Profit has to be assumed in any appraisal, its level is closely correlated with risk. The greater the risk, the greater the profit level, in part as a contingency against the unexpected.

- Ultimately, the landowner holds the key and will make a decision on implementing the project or not on the basis of return and the potential for market change. **In this case, creating market change is central to the financial outcome**.

2. **Key Factors**

The key base values and costs in this case are all justifiable and not contentious. They have been thoroughly researched and are supported, at least at today's values and costs.

However, the issues are all about **Future Net Capital Growth**, **NOT** today's situation.

The influential factors are as follows.

2.1 Historic Agreements

The simple fact remains that this proposal has been and always was driven by its legacy. Its history via various agencies including English Partnerships, the HCA, the Treasury, TFL and ultimately the GLA, has inevitably meant that some agency, or several, will receive significant sums via the original land agreement, and currently, none, it would appear, are prepared to re-cycle any share of those receipts back into affordable housing in Greenwich. That is a key driver in this case. Before February 2014, when Government largely abandoned grant aid to affordable housing, we would have expected most schemes to have exceeded 30% affordable housing. Without grant, that expectation has now been reduced by about one third.

2.2 Infrastructure Costs

A second key driver in this case is infrastructure costs. Historically, there was considerable expenditure on clearing and decontaminating the area but much of this was superficial. The revised proposals involve substantive costs and these are complicated by the need for existing parking areas for example, to be replaced in order to release those areas, together with a new public transport interchange and other requirements, all of which are pre-requisites to development phases, and thus a major factor in determining cash flow. Put simply, the financial effect of heavy up-front infrastructure investment, is to defer a positive return for some years, and thus increase the risk associated with the scheme.

2.3 Value v. Cost inflation - Current Deficit

We have examined in great detail the evidence submitted by the applicants and their advisors and accept the broad premise, namely that the proposals, even on the much expanded basis, remain in the medium term, in deficit, and that that deficit is in excess of £1bn. The key therefore is the ability of the proposals to not only ‘make a market’, that is deliver a ‘place’ in North Greenwich which generates a ‘new’ market more akin to Canary Wharf in value terms, but to do so taking account of build cost inflation over what is a very protracted build period. This is clearly a very high risk strategy.

2.4 Affordable Housing

Nevertheless, despite the risk involved, the applicants have committed to deliver a guaranteed 25% affordable housing element in the overall scheme, albeit this element contains 22.7%. Despite earlier contributions, the current revised masterplan assumes a no grant regime and as noted above, there is no doubt in our view that this approach exacerbates developer risk.

3.0 Conclusion

The result therefore and what has been the subject of intense discussion between RBG officers, ourselves and the applicants, focusses on risk, and in particular, what is the likelihood of the scheme being delivered as presented, and further, what expectation is there that the guaranteed overall 25% affordable housing element (22.7% in the current application) can be increased via Review mechanisms in the Planning Agreement, which the applicants are committed to ?

In response, it has to be emphasised that both the applicants and ourselves are inevitably speculating, not only regarding the extended length of the project but also the potential for a wide range of possible changes in the future to delivering major projects and affordable housing. As such, in line with standard development appraisal conventions, all parties have accepted that we can only model future potential based on current costs and values as a benchmark and then extrapolate accordingly. RBG officers and ourselves have required the applicants and BNParibas to consider those possibilities which they have done. Their summary of potential is attached to this letter. (See below). BNParibas conclude as follows:

> Our analysis indicates that should sales prices increase with those achieved at Woolwich Arsenal, the proposed development at the Greenwich Peninsula may be in an economically viable position to provide **additional** affordable housing **half way** through the proposed development period of 20 years. This is as a result of our analysis showing that should 5% net growth be achieved the **current deficit existing within the proposed scheme will be cleared and an IRR of 19.77% may be achieved by year 10**. Should a net increase exceed the Woolwich Arsenal development, additional **affordable housing could potentially be provided within the first 10 years of the development period**.

As officers are aware, we have debated this assessment at length with the applicants and it is our professional opinion, that there is a strong likelihood that the BNParibas conclusion will be achieved, in which case, the Peninsula proposals, without further grant or GLA financial support, will exceed the applicants guarantee of 25% affordable housing. Since apart from Registered Provider sites, that would be unusual in London, we are obliged to support the submission.

Yours sincerely,

C.D.Marsh FRICS MRTPI