Submission Relating to GL Hearn 250dpa Viability Assessment (EXD084)

Matthew O'Connell, March 2020

I have a number of summary comments to make in relation to this GL Hearn ("GLH") assessment:

1. Lack of Relevance

GLH's assessment relates to 8,300 dwellings, rather than the 10,000 which are included in the NEA Local Plan.

As a simple but important point, this means that **the assessment is not technically able to demonstrate viability for the Local Plan**.

Aside from the technical inapplicability, the different dwelling numbers are – of course – significant in a practical context: for example, the RTS is a fixed cost, identical for 10,000 and 8,300 dwellings. So while GLH works on a per dwelling infrastructure number similar to Hyas (before contingencies are considered), **actually the per dwelling infrastructure number would need to be higher.**

2. Incorrect Infrastructure Phasing

As with other private sector developer viability analysis**, the infrastructure phasing is much later than it would need to be to be compliant with the Plan policies** (RTS is a simple example).

For example, **around 50% of the Hyas infrastructure spend is in the Plan period, but only 30% of the GLH infrastructure spend is in the Plan Period**.

The infrastructure phasing is also simply a straight-line, £1.1m per month, whereas in reality there would be larger initial sums in the early stages. This is a highly flawed simplification (on which see implications set out below)**, and we note that it means also that the infrastructure phasing shown bears no resemblance to the Local Plan evidence base (e.g. Gleeds).**

3. Optimistic Assumptions re Contingencies

Infrastructure contingencies are 10%. **There has been no sensitivity analysis relating to the higher contingencies requested by the Inspector.**

4. Interest on Land Purchase Problematic

While GLH claim to have reflected interest on land purchase in their analysis, the interest credit of £40m compares to Hyas' interest cost £309m, **a remarkable difference of £349m**.

This is driven by 3 key factors:

1) The flawed assumption, discussed at length by Mr Sunnucks at the EiP, that there will be – according to the model – **no developer/investor profit payout until the end of the project**. While this might work in short term projects (5 years maximum), it is clearly unrealistic for 40+ year projects to withhold profit for many years as no rational developer/investor would accept this. **This flawed assumption heavily understates the debt balance for a significant portion of the project**

2) The credit interest applied to cumulative cash is 0.5% (note that no other viability analysis has had credit interest applied). **This is very impactful as the profit which is incorrectly "held" in the project over the long term earns positive interest when in reality that profit would be paid out**. This distorts the interest calculation hugely (note the Hyas figure) such that it lacks any real meaning in context.

3) The slow and straight-line infrastructure phasing means that **the debt balance earlier in the project is artificially low**, further distorting the interest calculation

   We specifically note in this context (and indeed relating to (2) above) the UDC Inspectors' comments (para 64 in EXD078) that:

   "There would be in the early years, disproportionately high infrastructure costs. Therefore, we are concerned that the cost of interest from borrowing and particularly peak debt has not been factored in at an appropriate level"

Overall, and this will likely be obvious to the Inspector, the GLH modelling is technically flawed with regard to debt / interest. Modelling – and the ability to rely on that modelling – requires sensible and justifiable assumptions; **the GLH analysis does not clear that threshold, most significantly because of the points raised in this section, and therefore cannot be relied upon at all.**

5. IRR Output Cannot be Relied Upon

There is no indication of how the IRR analysis is carried out, but **the figure of 61% clearly looks very strange** in the context of the discussions elsewhere in the examination of 12-20% being a developer target range (and indeed the IRRs shown by NEGC being well below such a viable range (we note again that the Hyas IRR calculations are totally flawed hence we only refer to the NEGC IRRs in this context)).

An IRR is calculated as a time-adjusted return achieved on funds invested. **The serious flaws in the GLH approach to infrastructure / cashflow / profit and therefore the understated debt balances mean the implied funds invested are artificially low.** This artificially inflates the IRR to the 61% quoted. This output clearly cannot be relied upon.

6. Residual Land Value Nevertheless Only Shows Marginal Viability

GLH have previously provided a £100k BLV (September submission), which is broadly in line with the £100-150k BLV range cited by others, and supported by the UDC Troy report's £100-127k range for A120 Corridor Garden Communities (all figures per acre).

Due to the basic technical errors relating to profit payout / debt / interest, the RLV quoted is slightly higher than for the 300dpa scenario (£118k vs. £114k). **This in itself shows the flawed nature of the analysis as clearly a lower delivery rate will produce a lower RLV whereas we have the opposite here**.

Even if an RLV of £118k were a credible figure rather than being undermined by the modelling errors, nevertheless it does not demonstrate viability anyway as **it clearly fails to take into account Harman Guidance** (p16) that *"Given the clear emphasis on deliverability within the NPPF, Local Plan policies should not be predicated on the assumption that the development upon which the plan relies will come forward at the 'margins of viability'"*.

Harman guidance was the prevailing Local Plan viability guidance at the time this Plan was prepared and therefore must be taken into account fully. **£118k/acre is clearly marginal relative to a benchmark of £100k/acre and therefore the site has not been shown to be viable**.

We note that the UDC Inspectors commented on the problematic nature of marginal viability in their letter, **and indeed determined marginal viability for A120 corridor garden community sites to be in the approximately £150k/acre context.**

7. Conclusion

This paper shows that the GLH viability analysis for West of Braintree cannot be relied upon. The dwellings number used is wrong; the infrastructure is too low and is also straight-lined rather than weighted upfront as would be required; contingencies are inadequate; a flawed assumption about 40 year retention of profit and credit interest earned on that profit renders the interest calculation meaningless; the bizarrely high IRR demonstrates the flaws in the analysis; and even if the modelling were considered credible, the RLV of £118k is not beyond the "margins of viability" as required by Harman guidance.