Case study: St. Mary's Residential

We can thank the determined and dedicated efforts of a Southwark-based voluntary monitoring group – the 35% campaign – for opening a real window on the real world application of development viability testing. The group forced Southwark council, following a prolonged legal process under the freedom of information (FOI) laws, to release into the public domain viability appraisals covering local multi-storied regeneration developments that had been previously kept secret on commercial confidentiality grounds.

One such scheme was St. Mary's residential in the Elephant and Castle. It involved the redevelopment by the australian property firm, Lendlease, of a 0.36 hectare mixed use site, which included a former council owned swimming pool, into a 37 storey residential block and pavilion. 284 dwellings were provided with some subsidiary retail and commercial uses.

Savills, a leading property industry consultancy in July 2012 submitted a development viability appraisal to Southwark council on behalf of Lendlease. It concluded that the insertion of any on-site affordable planning obligations within the scheme would render it unviable.

Assumptions made within the appraisal included a:

- site land value of £12.5m – based largely on estimated comparable values of residential sites earlier developed in Southwark, including the strada and king's reach tower;
- developer profit of 25% on GDC;
- residential market value of c£129m - £638 per sq.ft (spf).

In reality, Southwark sold the site to Lendlease for £6.6m, just over half the land site value that was inputted into the residual appraisal model submitted.

The scheme GDC outturn was £108m, which included the £6.6m that Lendlease actually paid to Southwark for the land site, and the firm's £3.5m contribution to the borough towards a replacement leisure centre in lieu of any affordable housing obligations. £79m of the total GDC was accounted for by build costs. Finance and other costs made up the remainder.

The units were actually sold for a total of £209m, at an average of £1,033psf. Three penthouse suites alone accounted for £8.3m of that total.

The resulting excess of realised GDV over GDC, as reported by Lendlease to its shareholders, generated a scheme profit of £113m. £12.2m of that was remitted back to Southwark as overage– or profit share. Lendlease was left with a net profit of c£101m.

The realised profit actually, therefore, only just fell short of the scheme GDV, suggesting that the realised Lendlease profit rate relative to GDC was over 90%, rather than the 25% assumed in the appraisal.

On the face of it, a mind-boggling fleecing of a gullible inner London LPA, apparently beguiled by comforting PR talk of ‘partnership’ from a sophisticated and experienced property multi-national.

That harsh judgment should, perhaps, be put in scheme-context. Southwark’s aim was to generate receipts, rather than to achieve affordable housing on the site. At the end of the day, it realized c£22.5mn directly from Lendlease, excluding a CIL contribution of c£1m and other sundry other received receipts. The council also, of course, got the site developed.

But the overage of £12.5m that it obtained represented only c12.5% of total scheme profit. A proportion closer to 50% would appear to have been much more appropriate.

An additional overage of c£38m could have possibly financed the building of additional c100-500 affordable units within the borough, depending on their size, tenure, the financing model used, and whether the council was able to offer public or other land secured at below market levels.

Meanwhile local residents could still have enjoyed the new leisure centre facilities and the emerging mini-manhattan ambience of the newly-regenerated emerging elephant and castle neighbourhood. Lendlease, in turn, could still have enjoyed a c.50% return relative to scheme GDV: more than twice that assumed in the appraisal, already at the upper end of normal expected industry returns.

Putting that into perspective, in 2015-16, 324 additional new build affordable dwellings were supplied in Southwark, of which 109 were reported as derived from section 106 agreements.