Introduction

This note provides a response to the BNP Paribas Real Estate ("BNPP") note provided at Appendix 4 of the OPDC's written response, provided on Friday 5th July.

In light of the limited time available to Old Oak Park Ltd ("OOP") to respond to the additional documentation provided by the Old Oak and Park Royal Development Corporation ("OPDC") this note addresses only what we consider to be any key matters in relation to this new and updated valuation feasibility study prepared by BNPP.

This note should be read in conjunction with the covering Overview Note prepared by Town Legal dated 16th July 2019.

Site and development tested

There is a disagreement between the parties in respect of the size of the site being tested. BNPP exclude site Allocations 3 (Triangle Business Centre) and 28 (Cumberland Business Park, ("Cumberland")). Paragraph 6.4 of the OPDC's covering note suggests that these two parcels of land have been excluded because "…Cargiant neither has a freehold interest in the entirety of these sites nor are they occupied by Cargiant or considered to be operational land for the purpose of Cargiant's business". Within the BNPP note it states at paragraph 2.2 "The latter two sites propose the delivery of significantly less housing units and we consider that they are adequately covered by the testing undertaken in the Whole Plan Viability Study".

We address these comments below:

- Cargiant do not own the Triangle Business Centre ("Triangle") but do have a long leasehold interest in the property of 91 years. As such, they are considered to "control" the site in the short to medium term, or at least for as long as is required to be considered under the Local Plan period;
- Site Allocation 3 includes includes Cargiant's SMART Repairs Workshop and the Quality Control Test track, both of which are Cargiant operational land;
- The OPDC refer to the non-operational land as "investment" properties, however, this is a misnomer. The land at Triangle (and the Gateway Trading Estate ("Gateway") which is included in Site Allocation 2) was specifically purchased for expansion and was to be rented out until all the units were acquired. This has been an integral part of the business's strategy for the last 34 years since Cargiant came to the area, originally occupying only 2.7 acres, and a key part of its success. As a special purchaser considerable sums over market value have been paid by Cargiant to assemble this land over many years as the object was for expansion. The site's position adjacent to Cargiant was imperative for long term contiguous operation. If Cargiant was purchasing land simply for investment purposes, there would have been better opportunities elsewhere; and
- The size of Site Allocations 3 and 28 is irrelevant. Both form part of the wider Cargiant site, whether they are currently operational or purchases for future operations. The Inspector has requested a study of the Cargiant 'lands' (see amended agenda hearing session title) and thus it does not appear unreasonable to include Cargiant's future expansion sites.

At paragraph 5.2 of DS2's report (which formed part of OOP's written submission on 28th June) we raised a query about whether the commercial floorspace figures identified in the Site Allocation tables in the Local Plan are on a Gross External Area ("GEA") or Net Internal Area basis. BNPP have assumed

the latter, however, there will be viability implications if these are provided on a GEA basis (as is normal in planning terms). This query has not been clarified.

GL Hearn report

BNPP have again reiterated their earlier comments that the GL Hearn report (dated February 2018) be disregarded as part of this study. BNPP's reasons centre on the differences between the scheme tested by GL Hearn and the 'scheme' required by Site Allocation 2.

At this stage we cannot comment in detail, suffice to comment that it would seem incongruous for a scheme of 5,300 homes and 48,800 sq m of commercial floorspace (as tested by BNPP) not to include any community or leisure uses.

More pertinently, our primary comment as to the relevance of the GL Hearn report was in relation to benchmark land value, and as such unrelated to the nature of the 'scheme' being tested. At paragraph 3.25 of our report we noted that the GL Hearn report recognises that an Existing Use Value-based level of return to a landowner may not be appropriate when considering the viability of redevelopment of an operational business such as Cargiant, and as a result, relocation costs would form a reasonable element of the benchmark land value. The GL Hearn report was commissioned by the OPDC to consider the viability of the Cargiant site and as such, given the purpose of this study, its conclusions cannot be simply dismissed.

Benchmark Land Value

Overview

BNPP have written extensively in response to our comments about the Existing Use Value ("EUV") of the Cargiant site. We have responded where we can in the time available to us, however, we would reiterate our comments made in our report that whilst we have sought to address BNPP's original comments and assess the site's EUV, we actually attribute little weight to an EUV plus arbitrary (BNPP calls it "standard") premium scenario. This is addressed in our comments at section 6 of our report, but to reiterate the key themes:

- EUV is not always the determining basis of land value. It must be based on the site specifics. BNPP acknowledge this within the original Whole Plan Viability Study ("WPVS");
- BNPP have not actually sought to understand the true costs of relocation and whether their premium does cover the costs of moving the Cargiant business;
- BNPP's assessment does not consider a 'do nothing' option when considering the "other options available to a landowner" (PPG 2014, para 015) in arriving at a competitive return to said landowner. This is particulalry relevant given the profitability of the Cargiant business. If the value of the business is greater than the underlying value of the land 'use' then this must be a material consideration;
- Due to the practical and financial requirements of relocating the business, as expanded upon in the covering note, there is no reasonable prospect of availability from the landowner (see explanatory "Cargiant Land Ownership Note" provided by Cargiant and included within the material submitted by Town Legal as part of their Overview Note. As such, the only way to make the site 'available' and therefore 'developable' is through CPO powers; and
- There is no feasible relocation option, so availability can only be achieved through a total extinguishment of the business and these costs should form the determining basis for this study's benchmark land value.

Existing Use Value

Notwithstanding the comments above under the 'Overview' heading, we comment briefly on BNPP's EUV section.

- BNPP highlight their previous comments about the site's "restricted" access and secondary nature of the existing buildings, indeed they highlight that these comments are made within the CBRE report provided by OOP. They are correct that these same points are made by CBRE, but in the context of justifying their value conclusions of c. £5m per acre when compared to Park Royal at £6m per acre. It is not reasonable to take CBRE's comments out of context.

- BNPP note that a portion of the CBRE EUV valuation is based on a notional new industrial development which is considered to form an Alternative Use Value ("AUV") and therefore does not receive a premium. To avoid confusion, CBRE have been asked to omit any new development as part of their valuation (even if for continuing industrial use) and value on a bona-fide EUV basis (i.e. existing buildings). Their revised valuation report is being prepared, however, in summary returns a figure of £242m. This is only £18m lower than their original report and reinforces the conclusion that the value of the underlying industrial 'use' is what is driving values, as opposed to existing or new buildings.

- BNPP have arrived at a new EUV, which is in fact lower than both their original Benchmark 2 and Benchmark 3 as set out in the WPVS. What is strange is that Benchmark 2 and 3 were based on underlying rents of £8 and £9 per sq ft, at yields of 8% (see WPVS), however, we have previously established that rents at Triangle and Gateway are between £17 and £22 per sq ft, with yields at c. 5%. As such, it is difficult to reconcile this with a proposed figure that is below benchmarks 2 and 3 in BNPP's most recent note.

- BNPP have arrived at current day figure of £155.48m, or £2.82m per acre for the whole site (based upon their smaller site area of 17.22 ha). BNPP do not provide any comparable evidence to demonstrate whether this figure is robust or justifiable. In contrast, CBRE include a range of comparable data within their report.

Relocation costs

In relation to relocation costs BNPP have included new third-party advice from Deloitte. This is commented on within Town Legal's Overview Note, however, we would highlight the simple fact that Deloitte's estimated of the costs of relocating are considerably higher than the figure derived when applying a 20% premium to BNPP's EUV figure. While the Deloitte figure is not agreed, their methodology supports our position that, financially, an EUV plus arbitrary/ standard premium is not appropriate in this instance.

Extinguishment

As with relocation, BNPP are advised by Deloitte in regards to extinguishment costs. Their comments are again addressed within the Overview Note. In summary, the note comments that there is no 'double count' of the rental income when arriving at an EBITDA figure, and as a result, depending on the multiplier used the extinguishment costs vary between £507.72m (x8 multiple) and £627m (x12 multiple). Either way, the figures are hugely higher than BNPP's assessment of EUV plus premium. The divergence between these figures serves to highlight and reinforces the need to consider the site's unique circumstances rather than taking a generic approach.

Construction costs

BNPP are advised by WT Partnership who have commented on the build cost report provided by Core 5. Core 5 are still reviewing the WT response however, it would appear that BNPP have effectively 'cherry picked' the lower rates proposed by Core 5 for the residential (the major component) but then not adopted Core 5's rate for commercial or their contingency allowance. Core 5 have prepared a balanced view of the required costs, evidenced by the lower rate for residential, however, BNPP's approach appears to ignore this and adopt the best combination of assumptions which arrives at an overall figure which is broadly similar to their original position, but which is still c. £60m lower than the costs proposed by Core 5.

Sales values, growth and rates

Values & growth

Our advisor, Knight Frank is still reviewing BNPP's updated position on values, however, they have provided preliminary feedback and our combined comments are set out below:

- BNPP appear to be fundamentally changing their position on values; previously there appeared to be an agreed position (before any regeneration premium is added) reflecting a current day value equivalent to £750 per sq ft ("psf"), upon which short term growth measures were applied. The short-term growth measures were based on an average of different leading agent forecasts. BNPP now appear to be changing their position, instead adopting a rate of £1,000 psf which would be achievable in 2021. This change is based on references to a previous piece of research undertaken by Knight Frank at the end of 2017.

- The difference in values as of 2021 that this change in approach generates is significant; under BNPP's previous approach, applying two years' worth of average growth to £750 psf would result in a figure of £781 psf. BNPP have effectively uplifted their 2021 figure by 28%. We have set out Knight Frank's comments in relation to the relevance of their research to this study, however, it would appear optimistic to disregard an agreed current day value (and short-term growth) in favour of a historic, and generic research piece.

- BNPP have not addressed the principle of a 'double count' when looking at current day, new build values, and regeneration premiums which are derived from past performance of regeneration schemes over and above the local authority growth levels. This concern is amplified when considering BNPP's new approach which is to adopt a future, aspirational figure which, by definition, must include elements of both new build and regeneration premiums.

- A key tenet of BNPP's approach to values is the value attached to future infrastructure improvements and the ability to transform PTAL levels. In particular, within their original submission BNPP extolled the "benefit from the regenerative impact of a significant quantum of new development, infrastructure and placemaking having come forward within the surrounding area in the first five years of the plan [i.e. Phase 1A] and continuing to come forward thereafter". <u>However, in the OPDC's most recent submission on the 5th July 2019 the Inspector is now being asked to ignore the HIF bid, and in turn, Phase 1A. Any omission of HIF/ Phase 1A must however equally apply to their impact on value and the weight that BNPP can reasonably attribute to it within the viability study.</u>

- In addition to the weight placed on Phase 1A, BNPP also refer to value generation in regards the new Overground Station proposed at Hythe Road. We have highlighted the uncertainty around the delivery of the Overground station at Hythe Road, however, BNPP note that there is "no evidence to suggest that Hythe Road Station is now precluded from proposals for Old Oak North as planning policy supports its delivery". We would however refer the inspector to comments made by Liz Peace of the OPDC to the London Assembly's Budge & Performance Committee on 11th June, stating the following:

  "The position is that neither station currently is budgeted in TfL plans. According to TfL modelling, there is no transport need for Hythe Road station. From our perspective, we would like a station at Hythe Road, because we think it would create a better regeneration, you know, better access to public transport. So, we would have to make a decision as we move into our, sort of, phase 1B about whether we would expect a potential developer to fund the Hythe Road station, or whether there are other sources of funding for Hythe Road station".

  The above statement is clear that there is little reasonable prospect of Hythe Road Overground station coming forward. As such, it and its value impact should be omitted from the assessment of values. The second extract which has been emphasised relates to BNPP's assumptions about infrastructure burden which we address in more detail later within this note.

We have set out Knight Frank's initial feedback below:

- The Knight Frank London Development Hotspots report "*identifies areas across London where there is the **potential** for residential development values to outperform the wider market*". Knight Frank acknowledged that certain areas referenced in previous iterations of this report have failed to achieve the forecast levels of growth due to the broad range of factors influencing the success of these areas of opportunity. Old Oak Common is no different. As referenced by both parties, there are a number of important factors that will contribute to the success (and price growth) at Old Oak Common, including the timely and efficient delivery of the proposed transport & infrastructure improvements as well as a degree of political & economic stability.

- The report in question was written and produced in Q4 2017 but published in Q1 2018 and the estimated (potential) value of £1,000 psf was forecast for the end of 2021 – a 4-year period. However, since this report was produced, the residential development market has come under continued pressure as have values. This is largely due to the fact Brexit remains unresolved, the political landscape remains extremely volatile, with the potential of a general election later this year and the uncertainty of a labour government. Meanwhile, the Old Oak Common scheme is no further progressed, with varying degrees of uncertainty surrounding the delivery of the Elizabeth Line, HS2 and the Overground station – which Knight Frank clearly set out in the report as critical drivers for the potential growth. The forecast values were also predicated and conditional on "critical mass being achieved in timeframe", which currently looks unrealistic given the increasing pressure on sales rates. For the avoidance of doubt, critical mass is important in delivering a truly exceptional mixed-use environment, which is capable of driving values and achieving outperformance, however given the challenging current market conditions this needs to be carefully balanced with achievable rates of sale

given the risk of internal competition (within a scheme) and oversupply, which can significantly inhibit price growth.

- Knight Frank clearly stated in the report that any forecast figures were subject to the "risks posed to the property market by the wider economic and geopolitical landscape". In this case, we have reviewed our estimated forecast values for Old Oak Common and taken a more cautious position, based on our understanding of the market over the past 18 months and the wider uncertainty over the contributing external factors.

Sales rates

In relation to sales rates we make the following comments of the BNPP note:

- BNPP focus on off-plan sales, but we reiterate our previous comments that they do not consider the overall, annual absorption, and how this actually relates to the overall project timeframe. This is particulalry important when considering schemes with multiple phases;
- BNPP do not address the fact that our report referenced the OPDC's own Absorption Study which indicated 200 units per annum (or 300 units per annum across the entire plan area). Based on this level of absorption it would take between 20 and 31 years to sell (based on the different number of private homes from 25% to 0% affordable housing); and
- BNPP now refer to Built to Rent ("BTR") as a way of increasing annual absorption rates. It is widely acknowledged that due to the different models employed by BTR operators which focus on long term returns, the current day values of a BTR units is often lower than its market sale equivalent. If BNPP wish to rely on BTR as a way of increasing absorption, then the reduced value of BTR needs to be incorporated into the study.

Affordable housing grant

BNPP's justification for including the higher, Registered Provider ("RP") 'route' level of grant funding still appears to rely on the scale of the scheme and the no. of homes as an overriding justification; that RPs will act as a developer or procured to deliver the affordable homes. This in itself is not a justification as it cannot be guaranteed that traditional developers will not deliver parts of the site, and procure an RP partner to deliver the affordable homes only, in which case they attract no grant unless they are being provided over and above the viable level, which is not the case under the scenarios we are testing, i.e. we are testing the viable amount, not an extra-over provision.

BNPP refer to RPs who have a strategic framework in place with the GLA, who may be able to receive grant on every affordable home in their pipeline programme. We are currently discussing this point with RPs that we work with, however our initial understanding is that this to applies to units being developed by the RP themselves, not s106 affordable homes. As such, the same concern with BNPP's approach applies.

CIL

BNPP have not commented on our concerns about the reasonableness of assuming that a developer of the Cargiant site would be required to carry no infrastructure burden other than CIL contributions. This point is particulalry pertinent considering the OPDC's own comments about the funding of the Hythe Road Overground station and the weight in terms of values being given to the "transformational" effect of new infrastructure, yet no one appears to be paying for this. A further example would be that during pre-application discussions the OPDC reiterated that developers would need to pay for 50% of the HS2 bridge (labelled "HS2 Eastern Access Canal Overbridge" on the plan

included at paragraph 5.7 of DS2's 28th June written submission). This is illustrates (in just one example) our concerns about not including any explicit infrastructure cost within the Cargiant study.

Summary/ conclusions

BNPP have made a number of key changes to the study inputs in arriving at this conclusion or make a number of assumptions which we believe to be flawed. These are summarised below:

- Assessed the wrong site and area by omitting the Triangle and Cumberland site allocations;
- Their assessment of EUV is not supported by comparable evidence and has been arrived at without reference to the original assumptions set out in the WPVS;
- Assessment of extinguishment costs is incorrect as the rental income has already been deducted when arriving at the EBITDA;
- Have cherry picked the most viable combination of build cost rates when arriving at their constructions costs;
- Have fundamentally changed their position on sales values, placing greater weight on a historic piece of research which was a 'snapshot in time' rather than the previously agreed approach of using current day comparable evidence. This change has a significant impact on the overall viability of the scheme;
- Place extensive weight on the transformational effects of new transport infrastructure, including that delivered by Phase 1A and the new Overground station, the former which the OPDC themselves suggest is to be ignored and the latter which the OPDC/ TfL have confirmed will not be coming forward; and
- Do not include any allowance for the cost of new infrastructure, yet at the same time, relying on the positive value impact of the same.

BNPP conclude that under any benchmark land value scenario the scheme is technically viable, albeit at very low levels in an extinguishment scenario. which, as set out, we consider to be the primary land value scenario of merit when testing the viability of the Cargiant site. This in itself raises questions as to how 'realistic' the plan is given the OPDC's slavish alignment with Mayoral policy objectives; would the Mayor consider a scheme with only 5% affordable housing? We suspect not given recent experience of Mayoral decisions across London in the past couple of years.

Notwithstanding that, when the above bullet points above are subsequently addressed, the site remains significantly unviable, be it under an extinguishment scenario, or to a lesser extent, a relocation scenario.