Chief Executive's Office,
Shepway District Council,
Civic Centre,
Castle Hill Avenue,
Folkestone,
Kent, CT20 2QY

23rd February 2018

F.A.O: CEO. Mr A Stewart & Council Leader, Cllr. D Monk

Dear Sirs,

Proposed Princes Parade Development, HYTHE

Lately, I have been looking at a great deal of material relating to this potential Council project, which I understand is likely to be granted planning permission within the next few weeks. I realise that if Planning consent is granted, it does not necessarily follow that the Council will implement the scheme. There is certainly an expectation that it will go ahead, in view of the upbeat publicity the Council has released in various ways to promote its "showpiece" scheme concept. However, despite all the positive noises coming from the Council and though we are newcomers to the area, we are aware of a strong degree of resistance in the town to the scheme, although it could gain a Leisure Centre.

My purpose in writing to you now is to acquaint you with the outcome of my own viability exercise, which produces a very bad result. Indeed, far worse than I had expected given the unique seaside location and a kilometre of prime frontage. I gather the Council is yet to carry out, or publish its own independent viability test to justify committing itself to such a complex and awkward project.

I certainly consider myself competent to offer you an independent professional assessment, as I am a qualified valuation surveyor and have 40 years of experience in the instigation and delivery of dozens of major commercial projects throughout the U.K.

By way of introduction, my wife and I moved to the beautiful and unspoilt town of Hythe in 2016 as an act of finally retiring from a challenging career to fully concentrate on active recreation and relaxation. Initially, we just wanted to ignore the development nearby to us and to carry on regardless, but as a "pro-development " person, by instinct, I had to check out the economics for myself.

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This has involved quite a lot of effort on my part, so I trust you will take care to understand my conclusions and concerns for the solvency of our unit of local government going forward. However, the scheme is still only a concept and there is only a limited amount of useful information available at this point in time. But, I do think there is sufficient to carry out a “ball-park” analysis to see if the concept has the makings of a viable project. In due course, in the interests of fairness, I will email to the people organising the Save Princes Parade campaign.

I have been a General Practice Fellow of the Royal Institution of Chartered Surveyors for 30 years and have specialised in real estate valuations, property asset acquisitions and instigating major development projects. This included having personal responsibility for leading the entire process, for delivering the completed project and having the ultimate financial responsibility at Main Board Level, in a Development Director role. An outline of my career is attached in Appendix D.

During my career, I have certainly run into resistance and opposition during implementation on a couple of major projects and have had some very scary times following unexpected construction delays and cost hikes. Fortunately, I managed to extricate my company and myself with just “cuts and bruises” plus some shame and embarrassment. So, I do identify with your present position, or dilemma.

From this point in the letter, I will endeavour to explain my approach to ascertain the scope there is to exploit this unique area of open land and produce financial, housing and leisure activity gains for our community. The latter facility being sited so close to our home would be, selfishly, an attractive prospect. Although I do have strong views on the limitations within the design of the “Centre”, they could just be academic now, or maybe there could be another time to offer my comments.

The Scheme: I have focussed totally on the Tibbalds design document dated August 2017 and have not attempted to change anything. Increasing the internal areas of the housing units slightly and assuming a luxury specification being the only exceptions.

Subsidised Housing Content (Affordable Homes): I have disregarded this purely for the purposes of establishing the highest property value at the outset before ascertaining what capital value discount the created market value might bear. But as you will see, there is not enough created surplus value to provide scope for a section 106 contribution as a further benefit.

Appendix A: this sets out my calculation of the maximum completed value of the residential element, i.e. the “Gross Development Value” (GDV) by aggregating all the anticipated private treaty sales receipts at full asking price. You will note that this totals £70 million, of which £2m is the capitalised rental from the commercial space and £68m is from residential sales.

Risks to Maximising GDV: Prospective purchasers and their Mortgagees will inevitably express concerns on at least two major issues and require both the

Developer partner and the Council to offer details of protective design features, warranties and guarantees from the outset.

These issues are:-
(1) the strata of contaminated landfill upon which their personal asset would stand and
(2) the technical solutions to absorb collected volumes of floodwater from over-topping waves in the sea and rain storms.

These complications would certainly deter some would-be buyers and others will seek a large discount on the asking price. This is likely to slow down sales completions and reduce the level GDV achievable, further reducing scheme viability.

Contracting Out or Passing-on of Risks: If it is believed or hoped that the Council can require its Developer Partner to take over undefined future claims and settle them at its own expense, then I contend this is very mistaken expectation. Successful developers are absolutely risk averse and always leave inherent, unquantified risks with the landowning partner. They will only recognise claims related to the quality of the building contractors work. The big firms survive and prosper by not falling into the traps Carillion recently have.

Funding & Cash Flow: the rate at which sales receipts can be banked will lag considerably behind the rate at which the contractor earns stage payments.
In aggregate, by the development completion date, I estimate some **£80m expenditure** of an estimated £99m overall developments costs would be certified for payment in monthly stages after 2 years. See Appendix B for the composition of the latter figure, it covers the £73m overall building costs, plus the fees and finance charges.

However the rate of sales completions on 150 homes ultimately targeted to yield an estimated total eventually of £68m, is unlikely to exceed a sales value of 75% by the end of year 2, i.e. around only £50m. Whereas the expenditure would be at £80m and rising quickly, showing an adverse cash flow and a £30m final deficit.

This would become a major medium term financial burden and would greatly affect Shepway's freedom of action on all other projects and services. Additionally, I suggest a contingency fund is set up to cover unexpected and unplanned problems, disputes and claims.

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Appendix B: sets out my Residual Method of Valuation, based on the maximised level of GDV. By then stripping off the unavoidable cost stages, one by one, covering marketing costs, project finance interest, professional design fees and building construction costs, plus the Developers profit, I arrive at a residual amount. This sum represents the value of the land element and the price a notional purchaser would bid to acquire the land.

However, as a result of the need to heavily load the currently evolved scheme solution with a number of exceptional infrastructure cost items, i.e. the new road, the "soft" landfill area, the contamination, the main services, the land drainage and filtration installations, protecting the Royal Military Canal and building a public Leisure Centre, the residual value "has sunk completely into the mire". It demonstrates that even the luxury housing profit potential is insufficient to fully cover these exceptional costs for this "attractive" project to remain even a little bit in the black.

<u>The result I obtain is a vastly negative one, the order of **minus £30 million**, meaning that the Council would have a very large shortfall caused by having to finance the early stage enabling engineering and technical works, should the project go ahead.</u>

Even at a fraction of this debt level, the scheme clearly should not be undertaken. Despite the "attraction" of this high profile scheme, it does not work unless money is no object, which these-days is the preserve of Middle Eastern States and Russian Oligarchs. Not territory any UK government authority should get itself into.

Furthermore, this £30m loss is taking <u>the most optimistic view</u> of the project implementation process. Though unlikely to be so fortunate, it assumes that the Council/Developer does not run into serious physical trouble on site, because, as you will know, construction delays increase costs massively. Indeed, as Carillion's liquidators are still experiencing on Liverpool Hospital.

Without wishing to be alarmist, but to be absolutely clear, unless and until an alternative viability study proves mine to be very inaccurate or wrong, I believe to proceed now, would be reckless. In all likelihood it would soon attract Central Government intervention at some stage before, during or after the event and culpability then examined.

Appendix C: this schedules my educated guesstimates of the main cost headings to be included and allowed for within the overall main building contract. Of the total of £73 million, £25m relates to the inherent technical and engineering aspects as "major enabling works"; £11 million for the Leisure Centre; £35 million for the residential element building costs. It does not include the £16m of other development costs comprising the total £99m costs, as mentioned above and shown in App. B.

The latter comprises 12,000 sq. m. (internal area/13,700 sq. m. external) for homes and 2,960 sq. m. Leisure Centre. Additionally, say 5 Hectares of paving and hard/ soft-scaping, estate roads, street lighting, etcetera.

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So, finally, what action could save the scheme and fix the viability problem?

Regrettably, the GDV is already at maximum and even an unachievable increase of 10% would do little to bridge the cost gap.

To enable proper measures costings to be prepared, the Council will have to spend up to another £2m in detailed design fees, but the cost savings would have to be dramatic to eliminate most of the negative site value.

The engineering content, with close care might be achieved more economically but this would only be known at the end of the process. Equally, the reverse in terms of fortunes could occur, so I think little can be achieved to improve the assessment of viability.
The residential element costs might be trimmed down, but the very high average cost of £240,000 per unit figure reflects a number of factors, including the anti-flood internal design at ground floor level, the piled foundations and the need to have ultra-strong glazing on the sea facing elevations to resist blown stone impacts etc.

Again, even if a very large 25% reduction target could be achieved, say by scaling down the specification and maximum contractor economy measures, this would only reduce the deficit by £10m. Such a downgrading, would be visually apparent and adversely affect sales values and the GDV level. I doubt if this is a worthwhile or realistic exercise, either.

Summarising, on the gain side, the Council gets a smart but “small” Leisure Centre and Commercial space, together worth say £13m.

On the debit side, the Council has to find a subsidy of £25m to cover the abnormal site issues, and it secures no subsidised (affordable) housing content.

After offsetting the £13m gain, the deficit is still an enormous £17m, which even if Shepway has such funds tucked away somewhere, should be utilised only upon other viable developments, not lost in the landfill.

To me having wrestled with the figures, it all now seems like a bad dream and a great gamble for modest rewards. Food for much further thought and debate, I trust.

My draft letter was much longer, but I think I have really covered the subject quite fully and I apologise for the length of the submission. Hopefully, though, this length does reveal the shape of the methodology to make it fairly easy to follow and I also hope my input is timely. Happy to participate in a discussion, anytime, if desired.

Yours faithfully

Derek H Maynard