DEVELOPMENT VIABILITY FACTSHEET

Introduction

Delivering development requires the involvement of many parties. Their actions can have a significant impact on the viability of a development – ie whether it is capable of coming to fruition or not.

It is therefore important to have an understanding of the economics of development and an awareness of how our actions can impact on delivery. This document provides a brief outline of some key points.[1]

The aim of Commercial Development

The primary aim of commercial development is to make a return (profit) through providing built space. To secure this profit, developers have to meet the demand and requirements of end users - whether it is providing residential, commercial or leisure space. In order to develop the space, in most cases, different permissions/consents will be required before development can begin. It is the granting of these permissions (in particular planning permission), which results in an increased land value (sometimes referred to as "uplift"). The extent of the increase in value will be determined by many variables, for example, site location, market conditions, as well as the individual site condition and the scale and type of the proposed development.

What is 'viability'?

For development to actually take place on the ground, the value (revenue) generated from the development **must exceed** the costs of undertaking the development ("costs" include the developer's profit). If, however, the costs exceed the revenues, then the development would be considered to be unviable. Consequently, it would be unlikely to progress on this basis.

Why does viability matter?

Viability is the key factor which determines whether development proceeds or not. In the current climate, it is more important than ever that public and private sectors work together to deliver development on the ground. Delivering the right development, in the right place is crucial in supporting the Government's aim of increased sustainable economic growth. The construction sector makes a significant contribution to Scotland's economy, creating wealth and supporting jobs.

How is viability assessed?

There are different methods which can be employed to assess development viability; the general term for this assessment is 'development appraisal'. A development appraisal involves a cashflow analysis, which uses data (for example revenues and costs over the life of the project) to determine the profitability of the development.

The following factors are consistent in the assessment and need to be predicted as accurately as possible to allow for a meaningful appraisal:

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[1] Detailed information on development economics and viability can be found online at http://www.scotland.gov.uk/Topics/Built-Environment/planning/publications/LearningResources

- **Gross Development Value** (revenue from the end sale or from letting the completed development)
- **Development Costs** (cost of land, build costs, abnormal costs, professional fees, planning obligations, developer's profit, costs relating to obtaining finance)

<u>How can viability be affected?</u>

Development viability can be affected in many ways. For instance, falling house prices can reduce revenues. Equally, changes in the cost of materials can affect the build costs. Although the public sector has no influence over such factors, there are many ways in which the actions officials and elected members take can affect development viability. One example:

- In order for development to come to fruition, finance is required to be in place upfront, in order to meet the initial costs of the development. This finance is normally borrowed (sometimes called "debt finance") and incurs interest which accrues over time. Therefore, *any* delay in the development process, can result in developers having to increase the term of the loan secured. This results in greater costs, which can affect viability.

<u>How to contribute positively to viability:</u>

1) Develop a deeper understanding of development viability

Developing an understanding of the economics of development can help in discussions with applicants and can also assist in understanding when a development has viability issues.

2) Remain solution focused

Recognising how costs and demands can impact on a development's viability, is key in order to be able to respond flexibly, so that solutions can be delivered. A willingness to explore what scope exists to phase the payment of Planning Obligations, for instance, can assist. When considering solutions to reduce costs in order to aid viability, it is also worth thinking about the scope for revenues to be increased, for example, by increasing the density of the development.

3) Dialogue

Good communication with applicants can assist in the decision making process.
Asking applicants for greater clarity on the details of their proposed project, including identifying the pinch points, can enable good outcomes to be delivered.

4) Timely decision making

Good use of resources for both public and private sectors is more important than ever. Timely decision making can help to reduce delays, and consequent costs for all.

Read more: Development Delivery and Viability:
http://www.scotland.gov.uk/Publications/2010/12/23134428/0