



Waverley LEP Clause 4.4B

Valuation Assessment

Prepared for Waverley Council

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QUALITY ASSURANCE

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1 INTRODUCTION

HillPDA was commissioned by Council to assess the marginal financial benefits to development in relation to floor space bonuses granted under Section 4.4B of the Waverley LEP and to assess the financial costs to development (benefit to Council's Affordable Housing Program) from the direct provision of affordable housing apartments under the same Section 4.4E.

This report is divided in the following sections:

- Section 2 shows the method and results of quantifying the marginal revenue to development from the granting of bonus floor space.
- Section 3 shows the method and results of quantifying the marginal cost to development (benefit to Council's Affordable Housing Program) from the delivery of affordable housing over a three year lease term.
- Section 4 shows the ratio of benefit to cost and the adjustments to lease terms and floor space ratios to bring the benefit cost ratio towards the 2:1 target.

2 MARGINAL BENEFIT TO DEVELOPMENT

The marginal benefit to development from the floor space bonus is calculated as the marginal gross revenue less marginal costs on sales less the marginal costs of production.

Marginal Revenue

The principles of assessing marginal revenue are as follows:

1. Where there is a bonus on the height of the building then the bonus apartments will be on the upper most levels of the building. Alternatively it may be on the levels immediately below the penthouse and sub-penthouse levels (given that a premium may be attached to the penthouse and sub-penthouse levels – refer to diagram below).
2. The marginal value (or value of the bonus floor space measured in dollars per square metre) should not be less than average value (the building's total value divided by total floor area).
3. An acceptable method of measure is the difference between the total value of the apartments without the bonus floor space and the total value of the apartments with the bonus floor space.
4. In the example below a bonus floor space provides an additional increase in the internal saleable area of 14.9% through an increase of building height (one additional floor) plus a slight widening of the building. The result is an increase in the end value by 15.7%.

Figure 1 – Valuation of Hypothetical Floorspace Bonus

Building Without Bonus Floor Space				Building With Bonus Floor Space			
Level	Sqm	\$/sqm	\$m	Level	Sqm	\$/sqm	\$m
				12	300	16,000	4.8
11	300	16,000	4.8	11	425	15,200	6.5
10	400	15,200	6.1	10	525	14,700	7.7
9	500	14,400	7.2	9	525	14,400	7.6
8	500	14,100	7.1	8	525	14,100	7.4
7	500	13,800	6.9	7	525	13,800	7.2
6	500	13,500	6.8	6	525	13,500	7.1
5	500	13,200	6.6	5	525	13,200	6.9
4	500	12,900	6.5	4	525	12,900	6.8
3	500	12,600	6.3	3	525	12,600	6.6
2	500	12,300	6.2	2	525	12,300	6.5
1	500	12,000	6.0	1	525	12,000	6.3
TOTAL	5,200		70.3	TOTAL	5,975		81.3
				Margin	775		11.1
				% Increase	14.9%		15.7%

Source: HillPDA

5. Cost on sales should be deducted from the marginal gross revenue including GST at one eleventh (9.09%) of the gross end sale value and any other costs on sales such as sales commission and legal costs. Generally these costs will be no more than 3.0% of gross end sale value.

The result is the expected marginal net sale proceeds from the bonus floor space.

Marginal Cost

Marginal cost is the difference between the design and build cost of the proposal versus the design and build cost of a hypothetical building constructed to the maximum Base FSR.

1. Generally this would include the net increase in gross floor space, balconies and possibly some increase in car parking spaces and vertical circulation (lifts and firestairs).
2. Generally it would not include site costs such as landscaping, driveways, fencing, water detention, substation and external works as these costs are generally not marginal.
3. Marginal professional fees, application fees, finance costs, interest, marketing and advertising, etc should be included and are probably best calculated by pro-rata with construction costs.
4. Land purchase price, stamp duty and other acquisition costs, valuation costs, land holding costs such as land tax and rates shall be excluded as these are not marginal costs.

Indicative Marginal Profit

Marginal revenue less marginal cost equals marginal profit.

From several recent examples we have developed a range of likely marginal profit levels resulting from floor space bonuses. The table below shows a range of outputs. The cost side is fixed at \$370,000 for a 75sqm apartment. The revenue side ranges from \$12,000/sqm to \$18,000/sqm depending on location, views, etc. The upper end would refer to apartments near the top of high rise buildings with uninterrupted distant water views.

Table 1 - Typical Marginal Profit Levels for a 75sqm Apartment

(\$/sqm)	Typical Price	Net Revenue	Cost of Apartment	Marginal Profit
12,000	900,000	791,182	400,000	391,182
13,000	975,000	857,114	400,000	457,114
14,000	1,050,000	923,045	400,000	523,045
15,000	1,125,000	988,977	400,000	588,977
16,000	1,200,000	1,054,909	400,000	654,909
17,000	1,275,000	1,120,841	400,000	720,841
18,000	1,350,000	1,186,773	400,000	786,773

Source: HillPDA Estimate

The marginal profit for a 75sqm apartment is likely to range from \$390,000 to around \$780,000.

3 MARGINAL BENEFIT OF AFFORDABLE HOUSING

The marginal cost to development refers to the loss from providing the affordable housing apartments. Under Clause 4.4B the requirement is a minimum of 50% of the bonus floor space be provided for a minimum of 3 years at zero net rent.

The marginal cost to development is equivalent to the marginal benefit to Council's Affordable Housing Program.

The discount on the market value of the apartments that are to be given to affordable housing is the difference between:

1. the market value of the apartments without an affordable housing lease; and
2. the value with an affordable housing lease to an investor at the time of building completion.

It is assumed that the investor would receive no rental income during the term of the lease and would not be liable for any statutory outgoings (such as land tax, strata levies, Council and Water rates) and general repairs and maintenance during the period of the lease.

Again the value will vary depending upon location and other factors. We will assume that the lower priced apartments are the ones likely to be provided for affordable housing.

The discount on end value would be equivalent to the present value of the differences in cash flow streams between:

1. net rental income received from the apartments if leased at market rent over the first three years; and
2. net rental income from the apartments for affordable housing over the first three years – which in this case is Zero.

Present value would be calculated using a discount rate that reflects the current net rental yield of new residential apartments in the locality based on market evidence. An alternative is to use the Reserve Bank Official Interest Rate plus say 0.5% to 1.0% risk premium.

For this purpose we have assumed 3% per annum as a net rental yield. The gross rental yield in the current market for new apartments in the Waverley area is around 4.5% resulting in a net yield of around 3%.

The net rent on a new average sized 2-bedroom apartment with a car space is around 28,500 per annum based on a gross market rental income of \$825 per week as shown in the table below.

Table 2 - Gross Rent and Landlord Costs for Typical 2-Bedroom Apartment

	Per Unit
Market Rent / Annum	42,900
Less Managing Agent Fees @ 6%	-2,574
Less Vacancies & Maintenance @ 10%	-4,290
Less Strata Levy	-3,200
Less Council And Water Rates	-3,080
Less Land Tax	-1,200
Net Rental Income	28,556

Source: HillPDA Estimate

\$28,500 per annum over three years gives a present value of \$82,000 using a 3% discount rate. \$82,000 is the cost to the development for the delivery of a 2-bedroom apartment with car space for a term of 3 years.

Please note that this assessment has not considered tax implications. Rules on negative gearing, depreciation, GST and CGT can have impacts on the value of affordable housing units.

4 MARGINAL REVENUE AND MARGINAL COST

As shown in Section 2 above the marginal benefit to development of the bonus floor space for a 2-bedroom apartment is between \$390,000 and \$780,000. The marginal cost to development (benefit to Council's Affordable Housing Program) of 2-bedroom apartment for a three year lease is around \$82,000.

The ratio of 2 bonus apartments for one affordable apartment translates to a benefit cost ratio to the development of between 9.5:1 and 19.5:1 in the majority of scenarios in the current Bondi Junction market. Hence a hypothetical development in Bondi Junction would stand to gain 9.5 to 19.5 times more benefit than the benefit to Council's Affordable Housing Program. The ratio is higher for higher priced units - generally those apartments just below the penthouse levels in a high rise building with uninterrupted distant water views.

The achieved benefit : cost ratio to the development is well above the target ratio of 2:1. In order to bring the ratio closer to 2:1 either a longer lease term is required or a higher proportion of apartments should be provided for affordable housing. The table below provides the range of benefit cost ratios under varying lease terms.

Table 3 - Benefit Cost Ratio and Various Lease Terms

Lease Term (years)	Discount (\$)	Benefit Cost Ratio Range	
3	82,000	9.5	19.0
6	158,000	4.9	9.9
9	226,000	3.5	6.9
12	289,000	2.7	5.4
15	346,000	2.3	4.5
18	400,000	2.0	3.9
21	447,000	1.7	3.5

Source: HillPDA Estimate

As shown in the table above a term of 19 years or more would be required to bring the benefit cost ratio down towards 2:1.

Again we need to note that this assessment has not considered tax implications. Rules on negative gearing, depreciation, GST and CGT can have impacts on the value of affordable housing units. If investors are unable to enjoy the benefits of negative gearing with

longer term leases for affordable housing then the discount on end sale values would be much higher.

An obvious scenario would be for the developer to hold onto the affordable housing apartments during the term of the lease. Subject to specialist tax advice there should be some tax benefit to the developer by way of GST exemption beyond 5 years after building completion.

An alternative is to increase the proportion of affordable housing floor space to bonus floor space. The table below shows the results.

Table 4 – Benefit Cost Ratio by Lease Term and Affordable Housing Ratio

Term (years)	Range	Ratio of AH to Bonus FS			
		0.5	1	1.5	2
3	Low	9.51	4.76	3.17	2.38
	High	19.02	9.51	6.34	4.76
6	Low	4.94	2.47	1.65	1.23
	High	9.87	4.94	3.29	2.47
9	Low	3.45	1.73	1.15	0.86
	High	6.90	3.45	2.30	1.73

Source: HillPDA

As shown in the above table a ratio of Affordable housing floor space to bonus floor space of 1:1 or even up to 2.0:1 is more equitable for a term of at least 6 years or even 9 years (depending upon the marginal value of the bonus floor space).

APPENDIX A: RESIDENTIAL UNIT MARKET APPRAISAL

Bondi Junction is located 6km to east of the Sydney CBD. The area enjoys good access to transport infrastructure, beaches, parks and Bondi Junction major centre shopping precinct. Demand for units is very strong with a median unit price of \$733,000 in the 2013-14 financial year. Units have experienced 5.5% average compounded annual growth over the preceding 4 year period¹. The 2011 ABS census reveals that a very high proportion of dwellings are units at 62.1% of total dwellings.

Dwelling typology is characterised by well positioned high rise units, many of which enjoy panoramic harbour views from the natural ridge line. However a substantial number of these units are older stock and do not provide a good comparable to new developments. The main difference is the internal size and the high amount of strata facilities provided as a component of the development. These features tend to be less desired in the current market environment which is characterised by a high number of investors looking to minimise capital expenditure on strata levies.

Sales of Existing Apartments

A recent comparable sale was recorded at 1 Adelaide Street for a well positioned 2 bedroom unit with 2 car spaces and large balcony sold at auction for \$1.45m or \$17,682/sqm in November 2013. The unit is representative of what is expected on the top floors new buildings that enjoy distant views.

Table 5 - Recent Sales of Older Apartment Buildings

	Type	Internal Area	Sale Prices	\$/sqm Values	Average \$/sqm
42 Waverley Street Bondi Junction	1b	57.5	\$710,000	\$12,348	\$12,348
	2b	86	\$900,000	\$10,645	\$10,645
	3b	113-178	\$1,500,000-\$2,000,000	\$11,268-\$13,274	\$12,300
80 Ebley Street Bondi Junction	1b	37-53	\$485,000-\$647,500	\$10,707-\$13,108	\$11,893
	1b+s	69	\$930,000	\$13,478	\$13,478
	2b	87-107	\$785,000-\$812,000	\$7,589-\$9,023	\$8,306
1 Adelaide Street Bondi Junction	1b	45-59	\$520,000-\$645,000	\$11,025-\$11,851	\$11,458
	1b+s	65-78	\$700,000-\$765,000	\$9,870-\$10,769	\$10,320
	2b	82	\$1,450,000	\$17,682	\$17,682
	3b	106	\$1,650,000	\$15,567	\$15,567
2a Hollywood Avenue Bondi Junction	2b	83	\$850,000-\$1,250,000	\$10,240-\$15,060	\$12,028
	3b	101-102	\$1,000,000-\$1,555,000	\$9,900-\$15,196	\$11,640

¹ Residex Suburb Report, June 2014

79-81 Grafton Street Bondi Junction	2b	103	\$900,000-\$965,000	\$7,266-\$8,398	\$8,409
	3b	128	\$1,084,000-\$1,590,000	\$8,469-\$12,422	\$10,089

Source: Red Square & Hill PDA Research 2013

The above table reveals a typical \$/sqm range of values between \$11,000/sqm and \$12,000/sqm. However end prices can reach as high as \$15,000-\$17,000/sqm in some buildings with uninterrupted harbour views.

Sales of New Apartments

The most comparable finished unit development is "The Forum" located at 310-330 Oxford Street Bondi Junction, a development completed in December 2012. Above level 9 the development enjoys panoramic views of the city.

It is clear from the rates achieved on sales during 2013 that values are between \$10,000 to \$13,000 per square metre for the lower units that enjoy streetscapes and \$15,000 to \$17,500 per square metre for the upper floor units that enjoy views of the Sydney CBD, harbour and Ocean.

Table 6 - Sales 310-330 Oxford Street 2013

	Type	Internal Area	Sale Prices	\$/sqm Values	Average \$/sqm
310-330 Oxford Street Bondi Junction (Lower levels views) Streetscape	1b	46-48	\$555,000-\$690,000	\$11,563-\$13,021	\$12,645
	2b	75-86	\$875,000-\$965,000	\$10,714-\$11,392	\$10,523
310-330 Oxford Street Bondi Junction (Upper levels)	1b	48	\$640,000-\$713,000	\$13,333-\$14,854	\$13,958
	2b	79-90	\$925,000-\$1,325,00	\$11,709-\$14,722	\$13,218
	3b	122.5-127	\$1,550,000-\$2,150,00	\$12,205-\$17,551	\$15,408

Source: Red Square & Hill PDA Research 2013

All nine apartments in "Aria" at 5 Waverley Cres were sold with prices from \$11,600/sqm to \$16,964/sqm. The building was complete in November 2012. All apartments are large 3-bedrooms with 168sqm internal area. Some distant but limited views to the northeast are enjoyed on the upper levels².

² Colliers International Valuation & Advisory Services Pty Limited, March 2014

Pre-Sales

Several buildings have recently been pre-selling apartments including the Vue Apartments at 570-588 Oxford Street. Four 3-bedroom apartments, each 111sqm, were recently sold for prices ranging from \$16,500/sqm to \$17,133. The apartments were on Levels 13 to 16 and all have distant views towards the harbour. The apartments have high quality finishes, which will include Caesarstone benchtops, stainless steel finished kitchen appliances, frameless glass shower screens and ducted airconditioning³.

A couple of apartments were recently sold in the "Arcadia" building at 42-44 Waverley Street for \$10,500 and \$12,100/sqm. This is at the lower end of the price range in terms of dollars per square metre and reflects the size of the apartments (190sqm each) and having no distant views⁴.

Residential Rental Values

Bondi Junction enjoys particularly strong demand for rental accommodation and this is exemplified by the high proportion (51%) of rented dwellings recorded for the suburb in the 2011 ABS census data. Rental accommodation is in strong demand, and if correctly priced, rarely spends longer than 2 weeks on the market. NSW Housing has recorded a median 1 bedroom unit rental value of \$500/week and 2 bedroom unit value of \$633/week for the December quarter⁵.

The Forum building at 310-330 Oxford Street provides some comparable evidence in the lower floors to what is proposed for affordable housing in the podium levels of the development at 570 Oxford Street. A local leasing agent leasing many of the units commented that even without car parking the units were popular if appropriately priced.

Table 7 - Rental Values 310-330 Oxford Street

	Type	Internal Area	Car	Weekly Rental Values	Average Rent
310-330 Oxford Street Bondi Junction (Lower levels views) Streetscape	1b	46-48	1	\$575-\$650	\$600
	1b+s	60-75	0	\$650-\$700	\$650
	2b	75-86	1	\$775-\$950	\$800

Source: Real estate.com & Hill PDA Research 2013

³ Colliers International Valuation & Advisory Services Pty Limited, March 2014

⁴ Ibid

⁵ NSW Rent and Sales Report

The proposed affordable housing units would be expected to offer a similar level of amenity offering and outlook to those found in the podium level of the Forum building at 310-330 Oxford Street Bondi Junction. The expected weekly rental values are displayed in table 7 below. Note we could not determine as to whether parking would be provided with each unit and therefore have provided a price with and without parking.

Table 8 - Proposed Weekly Rental Values

Apartment Type	Internal (sqm)	No -Parking	With Parking
1 bedroom	50-60	\$575	\$625
1 bedroom + Study	60-72	\$625	\$675
2 bedroom	80-85	\$775	\$825

Source: Hill PDA Research, 2013

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