

FW: Merantum's demise

Louise Round <Louise.Round@merton.gov.uk>

Thu 17/12/2020 7:50

To: Chris Lee <Chris.Lee@merton.gov.uk>; James McGinlay <James.McGinlay@merton.gov.uk>

fyi

Louise Round
Managing Director, South London Legal Partnership
Gifford House, 67c St Helier Avenue, Morden, SM4 6HY
DX: 161030 Morden 3
Tel: 020 8545 3380



From: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>

Sent: 16 December 2020 18:47

To: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>; Louise Round <Louise.Round@merton.gov.uk>

Cc: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>

Subject: Re: Merantum's demise

Thanks Peter

Yours ever

Paul

Councillor Paul Kohler
Trinity Ward
Merton Council
Liberal Democrat Group

Any personal data or special categories of personal data than you have supplied for the purpose of dealing with your query will be processed in accordance with my privacy policy which is available [here](#).

From: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>

Sent: 16 December 2020 18:17

To: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>; Louise Round <Louise.Round@merton.gov.uk>

Cc: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>

Subject: Re: Merantum's demise

Hi Paul

I've asked the queson of our Leader who has promised to call me back.

Peter

From: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>
Sent: 16 December 2020 17:02
To: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>; Louise Round <Louise.Round@merton.gov.uk>
Cc: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>
Subject: Re: Merantum's demise

Hi Peter

Let's be a bit bolder!

Here's the chance to show how scrutiny can play an independent and constructive role in decision making. The fact that a meeting has not been postponed before, or that the executive have not invited scrutiny's involvement, are not in themselves sufficient to excuse us from pushing now for pre-decision scrutiny.

Why not raise the issue with Cllrs Allison & Munday at least as it's surely in their interests to have the options available to the sub-committee scrutinised before they make their decision.

Yours ever

Paul

Councillor Paul Kohler
Trinity Ward
Merton Council
Liberal Democrat Group

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From: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>
Sent: 16 December 2020 16:33
To: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>; Louise Round <Louise.Round@merton.gov.uk>
Cc: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>
Subject: Re: Merantum's demise

Sustainable Communities meeting on 8 December, and could have undertaken pre-decision scrutiny then if invited to do so. I haven't checked with Cllr Mundy, but as far as I know he was not asked to include it on the agenda. Make of it what you will, but I infer that PDS was not considered. I can't recall any council meeting being cancelled or postponed once the agenda had been published, other than for reasons of *force majeure*.
To extend your footballing analogy, we must prepare for the kick off.
Peter

From: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>
Sent: 16 December 2020 15:49
To: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>; Louise Round <Louise.Round@merton.gov.uk>

Cc: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>

Subject: Re: Merantum's demise

Could we not negotiate with Cllr Allison to put the sub-committee decision back a couple of weeks early in January? Is there any commercial imperative driving this date? It strikes me that a decision like this should be subject to pre decision scrutiny to avoid it turning into a political football.

Yours ever

Paul

Councillor Paul Kohler
Trinity Ward
Merton Council
Liberal Democrat Group

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From: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>

Sent: 16 December 2020 15:44

To: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>; Louise Round <Louise.Round@merton.gov.uk>

Cc: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>

Subject: Re: Merantum's demise

I agree - but there's no meeting to arrange it. Scrutiny means require agendas to be published 5 days in advance.

Peter

From: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>

Sent: 16 December 2020 15:22

To: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>; Louise Round <Louise.Round@merton.gov.uk>

Cc: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>

Subject: Re: Merantum's demise

Thanks Peter - is this not something where pre-decision scrutiny might not be the more useful mechanism?

Yours ever

Paul

Councillor Paul Kohler
Trinity Ward
Merton Council
Liberal Democrat Group

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From: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>
Sent: 16 December 2020 15:15
To: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>; Louise Round <Louise.Round@merton.gov.uk>
Cc: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>
Subject: Re: Merantum's demise

Paul

The decision will be taken at the meeting of the Merantun Development Ltd sub-committee on Monday 21st December. The call-in must then be made by 12 noon on the third working day following publication of the decision - by my calculation that's Christmas Eve!

Louise, thank you for your swift and unequivocal advice.

Peter

From: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>
Sent: 16 December 2020 13:49
To: Louise Round <Louise.Round@merton.gov.uk>; Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>
Cc: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>
Subject: Re: Merantum's demise

I think we would be failing in our responsibilities if the matter was not call-in and propose that we do forthwith

Yours ever

Paul

Councillor Paul Kohler
Trinity Ward
Merton Council
Liberal Democrat Group

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From: Louise Round <Louise.Round@merton.gov.uk>
Sent: 16 December 2020 13:27
To: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>
Cc: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>; Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>
Subject: RE: Merantum's demise

Dear Peter,

As we have discussed at the constitutional working group, any decision made by the Cabinet, whether key or not is subject to call in. Under rule 16(d) of the Overview and Scrutiny Procedure Rules, this includes those decisions made by cabinet committees which in my view includes the Merantun Sub Committee.

So the short answer is yes.

Best wishes

Louise Round
Managing Director, South London Legal Partnership
Gifford House, 67c St Helier Avenue, Morden, SM4 6HY
DX: 161030 Morden 3
Tel: 020 8545 3380



From: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>
Sent: 16 December 2020 12:34
To: Louise Round <Louise.Round@merton.gov.uk>
Cc: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>; Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>
Subject: Fw: Merantum's demise

Dear Louise

The decision to wind up Merantun comes as a bolt out of the blue. In your opinion, is it liable to call-in, as a Cabinet decision would be?

Kind regards

Peter

From: Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>
Sent: 16 December 2020 10:58
To: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>; Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>
Subject: Re: Merantum's demise

Dear Paul

I learned of this decision only last night. I am not aware of any scrutiny taking place. We need to establish whether it is liable to call-in. I'll talk to Louise Round.

Regards
Peter

From: Councillor Paul Kohler <Paul.Kohler@merton.gov.uk>
Sent: 16 December 2020 10:22
To: Councillor Stephen Crowe <Stephen.Crowe@merton.gov.uk>; Councillor Peter Southgate <Peter.Southgate@merton.gov.uk>
Subject: Merantum's demise

Dear Stephen and Peter

Are you aware of any scrutiny regarding the recent decision?

I understand that some £1.3m was invested in this venture and I strongly believe we would be failing in our duties if we did not fully scrutinise these developments before it is too late to consider any alternative solutions to address whatever problem has been identified.

Yours ever

Paul

Councillor Paul Kohler
Trinity Ward
Merton Council
Liberal Democrat Group

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Impact of 1% interest increase for Merantun

Roger Kershaw <Roger.Kershaw@merton.gov.uk>

Fri 13/11/2020 15:31

To: Councillor Mark Allison <Mark.Allison@merton.gov.uk>

Hi Cllr Allison

You asked what the impact of the 1% PWLB interest increase for Merantun was.

On a straight annuity basis over 28 years calculates the extra cost at £3.4m.

However using the financial model on which our decisions have been made. The interest differenal is much larger at £8.2m. This is because the model uses cashflows to calculate the interest payable and because the net operang c ashflows are not sufficient to cover loan and interest repayment the debt rolls forward and consequently the interest owed is much larger over the period.

Thanks

Roger

 Print  Cancel

Model sensitivity analysis - additional slide

Oleg Pashkovskiy
<Oleg.Pashkovskiy@chas.co.uk>

Wed 11/11/2020 10:22

To: Paul McGarry <Paul.McGarry@merton.gov.uk>

Cc: James McGinlay
<James.McGinlay@merton.gov.uk>; Bindi Lakhani
<Bindi.Lakhani@merton.gov.uk>; Roger Kershaw
<Roger.Kershaw@merton.gov.uk>

 1 attachments (327 KB)

MDL CF SLIDES - Sensitivity.pptx;

Good morning Paul,

Please find attached an additional presentation slide summarising the results of the sensitivity analysis.

The text is can be edited on the slide.

Many thanks.

Kind regards,

Oleg Pashkovskiy
Corporate Finance Manager (CHAS /
Merantun Development)
Corporate Services
A: Merton Council, Civic Centre, London
Road, Morden SM4 5DX
E: Oleg.Pashkovskiy@merton.gov.uk
T: 0208 545 3367

Development cost query in original model and full presentation for review

Oleg Pashkovskiy <Oleg.Pashkovskiy@chas.co.uk>

Wed 11/11/2020 16:20

To: Roger Kershaw <Roger.Kershaw@merton.gov.uk>

Cc: James McGinlay <James.McGinlay@merton.gov.uk>; Bindi Lakhani <Bindi.Lakhani@merton.gov.uk>

1 attachments (6 MB)

PWC MODEL AS PER LAPC REPORT.xlsm;

Good afternoon Roger,

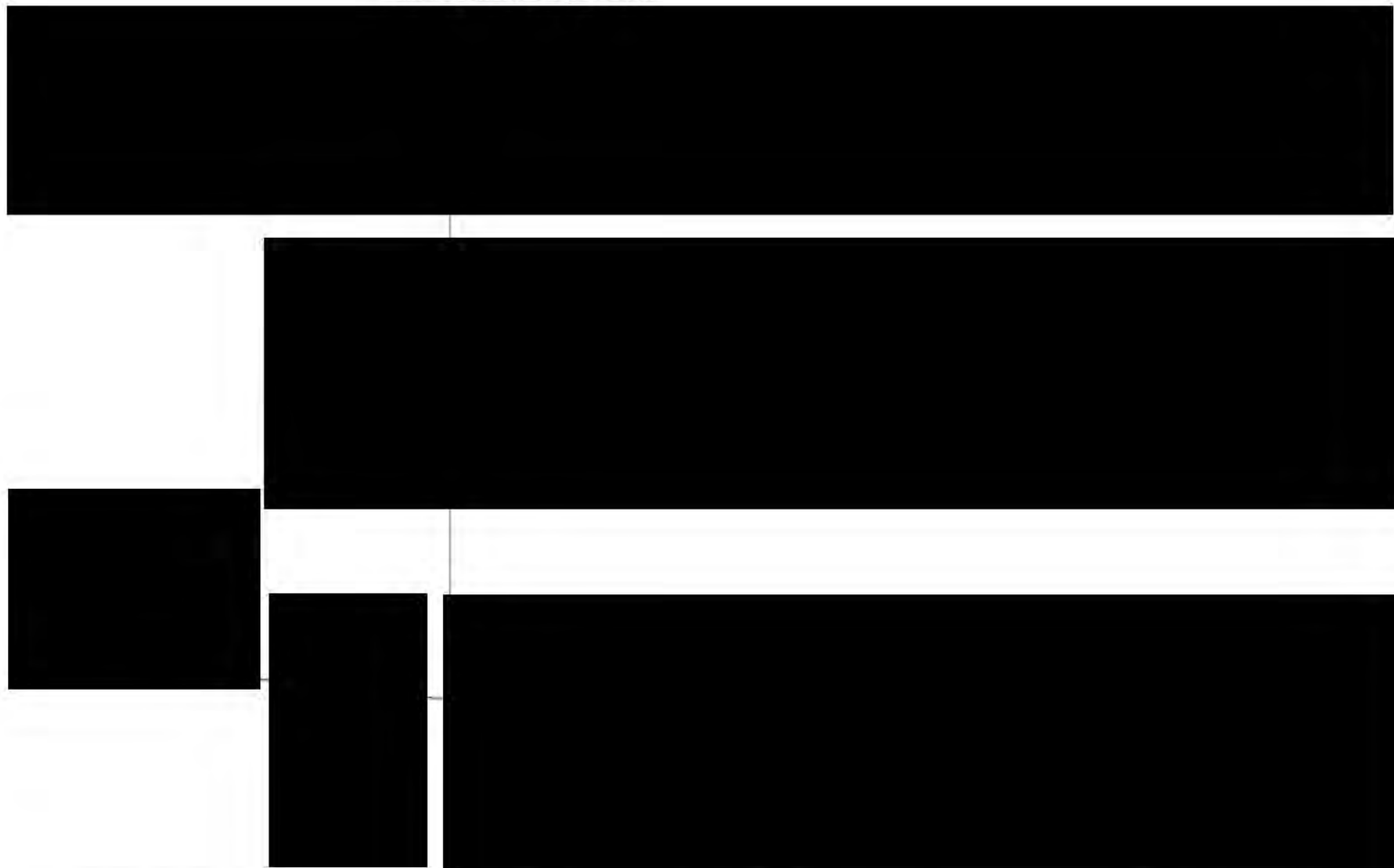
Many thanks for your query regarding Caroline’s question on the development costs in the original model.

Please find attached the original model – this is the version we managed to located within historic files which most closely matched the LAPC report.

Page 29 Here is the screenshot of the WOC CF tab which shows the development costs being as per presentation. The reason for the loan to WOC being £13m only is because a cash sweep set up was used and early sale proceeds were used to repay some of the principal as per the comments below:

	A	B	C	D	E	F	G	H	I	J	K	
1												
2	Year No.					1	2	3	4	5	6	7
3												
4	Start of Period					01-Apr-16	01-Apr-17	01-Apr-18	01-Apr-19	01-Apr-20	01-Apr-21	01-Apr-22
5	End of Period					31-Mar-17	31-Mar-18	31-Mar-19	31-Mar-20	31-Mar-21	31-Mar-22	31-Mar-23
15	In year cashflows (£000's)											
19	Sales profile (Private sale)											
30	Total sale cashflows											
31												
32	Sales profile (Affordable sale)											
43	Total sale cashflows											
44												
45	Sales profile (PRS)											
56	Total sale cashflows											
57												
58	Sales profile (Commercial sale)											
69	Total sale cashflows											
70												
71	Development cost profile (all units)											
72	Farm Road Church											
73	Canons Leisure Centre											
74	Elm Nursery											
75	Raleigh Gardens											

- 76 Site Name 5
- 77 Site Name 6
- 78 Site Name 7
- 79 Site Name 8
- 80 Site Name 9
- 81 Site Name 10
- 82 Total construction cashflows
- 83
- 84 **Rental cashflows (PRS)**
- 85 Rental income
- 86 Rental costs
- 87 Total rental cashflows
- 88
- 89 **Vehicle cashflows**
- 90 Vehicle operating costs
- 91 Vehicle one off development costs
- 92 Total vehicle cashflows
- 93
- 94 **PRE FINANCE NET CASHFLOWS**
- 95
- 96 **FINANCE CASHFLOWS**
- 97
- 98 **Senior debt finance costs**
- 99 Senior debt interest paid
- 100 Arrangement fees
- 101 Total senior debt financing costs
- 102
- 103 **Senior debt financing principal**
- 104 Senior debt draw down
- 105 Senior debt repaid
- 106 Total senior debt financing principal
- 107
- 108 **Corporation tax**



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Also, just to clarify, the finance slides will be added to the general presentation which will include some background information and the latest market insight.

Hope this clarifies Caroline's query.

Many thanks.

Kind regards,

Oleg Pashkovskiy
Corporate Finance Manager (CHAS / Merantun Development)

Corporate Services

A: Merton Council, Civic Centre, London Road, Morden SM4 5DX

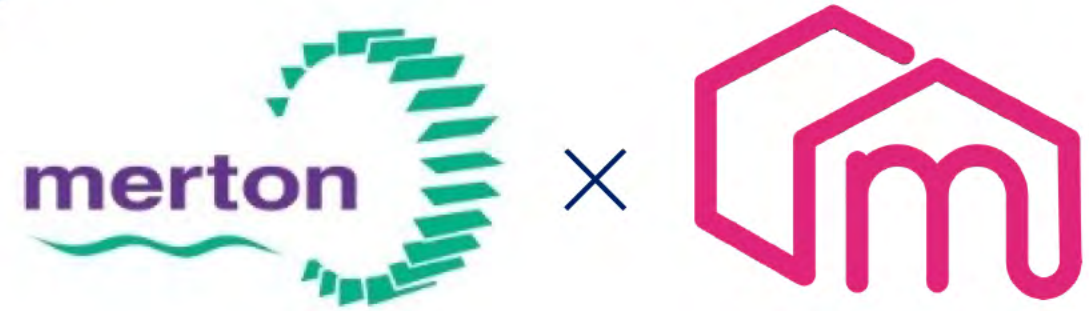
E: Oleg.Pashkovskiy@merton.gov.uk

T: 0208 545 3367

2020 MODEL SENSITIVITY ANALYSIS

Scenario in use	Base case - Jul 2020	Rent growth reduction to 2.5%	Rent growth reduction to 3.5%	LBM Borrowing rate increased by 1%	LBM to WOC interest margin increased by 1%	HPI decrease by 1%	Man & maint & lifecycle cost increased by 5%
PWLB drawdown	19,426	19,439	19,432	19,426	19,426	19,426	19,433
PWLB loan retirement	31-Mar-46	31-Mar-50	31-Mar-50	31-Mar-49	31-Mar-46	31-Mar-46	31-Mar-47
Loan to WOC	15,541	15,551	15,545	15,541	15,541	15,541	15,546
Cash equity in WOC	3,885	3,888	3,886	3,885	3,885	3,885	3,887
Land equity in WOC	4,970	4,970	4,970	4,970	4,970	4,970	4,970
WOC loan retirement	31-Mar-50	31-Mar-50	31-Mar-50	31-Mar-50	31-Mar-50	31-Mar-50	31-Mar-50
Cumulative I&E impact (project end)	31,852	16,808	24,717	26,363	32,947	24,224	31,166
Cumulative I&E impact (year 5)	1,665	1,481	1,582	1,078	1,792	1,535	1,620
Equity IRR (cash and land)	2.9%	(6.2%)	0.8%	1.1%	1.1%	1.4%	2.8%
Interest cover (max in year shortfall)	(636)	(944)	(655)	(804)	(804)	(636)	(651)

- **Changes in the inputs affecting the project over its lifetime have the most significant effect on the project profitability**
- **Adverse variations in short term variables like house price of 10 houses on sale after construction have relatively small effect and can be disregarded**
- **Any combination of adverse variations in the above factors will have even greater effect on the project profitability**



November 2020 update and next steps



OVERVIEW

- Progress
- Market
- Costs
- Financials





PROGRESS TO DATE

All four sites granted planning permission

- 21 flats for affordable rent
- 62 flats for private rent
- 10 houses for sale

MDL Board – review of Business Plan undertaken
MDL & LBM Shareholder workshop undertaken





Market rents and house sale prices

- Demand for PRS remains stable but softening in London as people don't need to commute as often to Central London
- Sales activity is buoyant with properties benefiting from reduction in stamp duty (March 21) – no benefit to MDL timeframes – again, stronger outside London
- Economic downturn will slow down sales and some people may look to renting rather than buying (FTBs)
- HPI – short term bubble





COSTS



COST NARRATIVE

The cost plan has inflationary allowances but, given the time lapsed, the cost plans would be subject to potentially further inflationary increases.

The tender market is temporarily heated in the short term, which could challenge our cost plans. There has been a lag in tenders issued which has now ramped up, and as a result contractors have much to price, leading to selectivity and upper pressure on cost.

This will flatten out in the mid-term (2021), and possibly depress depending upon what happens in the economy. The trend is for labour to deflate but materials costs to increase (Brexit).

Right of Light costs were additional to projected costs in the original 2017 MDL business plan. A number of options available but all add cost.

There would be potential for some value engineering further once a contractor is appointed.





FINANCIALS





ASSUMPTIONS (prior to review)

- LBM borrows all of loan to MDL from PLWB @3.5% and lends on @7.5%
- 30 year business plan
- Construction takes one year
- Interest starts from time of draw down of LBM loan to MDL but is rolled up for three years (until MDL income streams commence)
- MDL building does not build out Elm Nursery site



PROJECT CONTINUATION OPTIONS

Option	Est.Net present value, £m	Comments	Risk RAG
1. Project termination	(2.1)	<ul style="list-style-type: none"> - Sunk costs of the project wrap up - Planning permission obtained 	Yellow
2. Selling LBM land with MDL planning permission	(0.2)	<ul style="list-style-type: none"> - Utilisation of planning permission value added - Disposing of idle land plots - Value extraction at current asset state - Risk: finding a potential buyer 	Green
3. Develop and sell 3 sites and sell Elm Nursery to HA	1.9	<ul style="list-style-type: none"> - Utilisation of planning permission value added - Material value addition with potential gain - Risks: - material investment and financial commitments - sale value and timing uncertainties 	Red
4. Proceeding with 72 unit development	3.6	<ul style="list-style-type: none"> - Return: - £20m interest margin in 28 years - £12m dividend in 28 years - Risks: - material investment and financial commitments - sale value, rents and timing uncertainties 	Red



KEY MODELLING ASSUMPTIONS 2017 vs 2020 MODELS

Assumptions	APR 2017	JUL 2020	Change	% change
Private	2	10	8	400%
Affordable	20	0	(20)	(100%)
PRS	53	62	9	17%
Commercial units (trading space)	2	0	(2)	(100%)
Total units	77	72	(5)	(6%)
Unit sale proceeds	5,953	5,253	(700)	(12%)
Development costs	18,383	19,470	1,086	6%
HPI (% p.a.)	4.50%	2.00%	(3%)	(56%)
Rent (% p.a.)	4.30%	4.30%	0%	0%
Interest rates:				
PWLB loan to GF interest rate	2.76%	3.76%	(1%)	(36%)
GF loan to WOC margin	3.74%	3.74%	0%	0%
Borrowing rate	6.50%	7.50%	(1%)	(15%)

- Almost identical number of units
- £1m more expensive construction cost base
- Apr 2017 model assumed now “unrealistic” HPI level of 4.5%
- Annual rent increase of 4.3% might not be sustainable
- Borrowing is 1% more expensive in the new model



KEY RESULTS 2017 vs 2020 MODELS

Modelling results	APR 2017	JUL 2020	Change	%, change
PWLB draw down	16,278	19,426	(3,148)	(19%)
PWLB loan retirement	31-Mar-38	31-Mar-46		
Loan to WOC	13,022	15,541	(2,519)	(19%)
Cash equity in WOC	3,256	3,885	(630)	(19%)
Land equity in WOC	8,190	4,970	3,220	39%
WOC loan retirement	31-Mar-42	31-Mar-50		
Cum ulative I&E Im pact (project end)	67,451	31,852	(35,600)	(53%)
Cumulative I&E impact (year 5)	1,214	1,665	452	37%
Equity IRR (cash and land)	6.48%	2.94%	(3.5%)	(55%)
Interest cover (max in year shortfall)	(286)	(636)	(350)	122%

- Almost £2.5m more borrowing facility is required in the new model
- Land equity investment is reduced by 50% based on latest valuation
- New setting does not allow to repay loan to WOC early
- HPI reduction by 2.5% results in (£36m) lower cumulative I&E impact
- Project IRR reduced by half implying higher risk of producing positive NPV



2020 MODEL SENSITIVITY ANALYSIS

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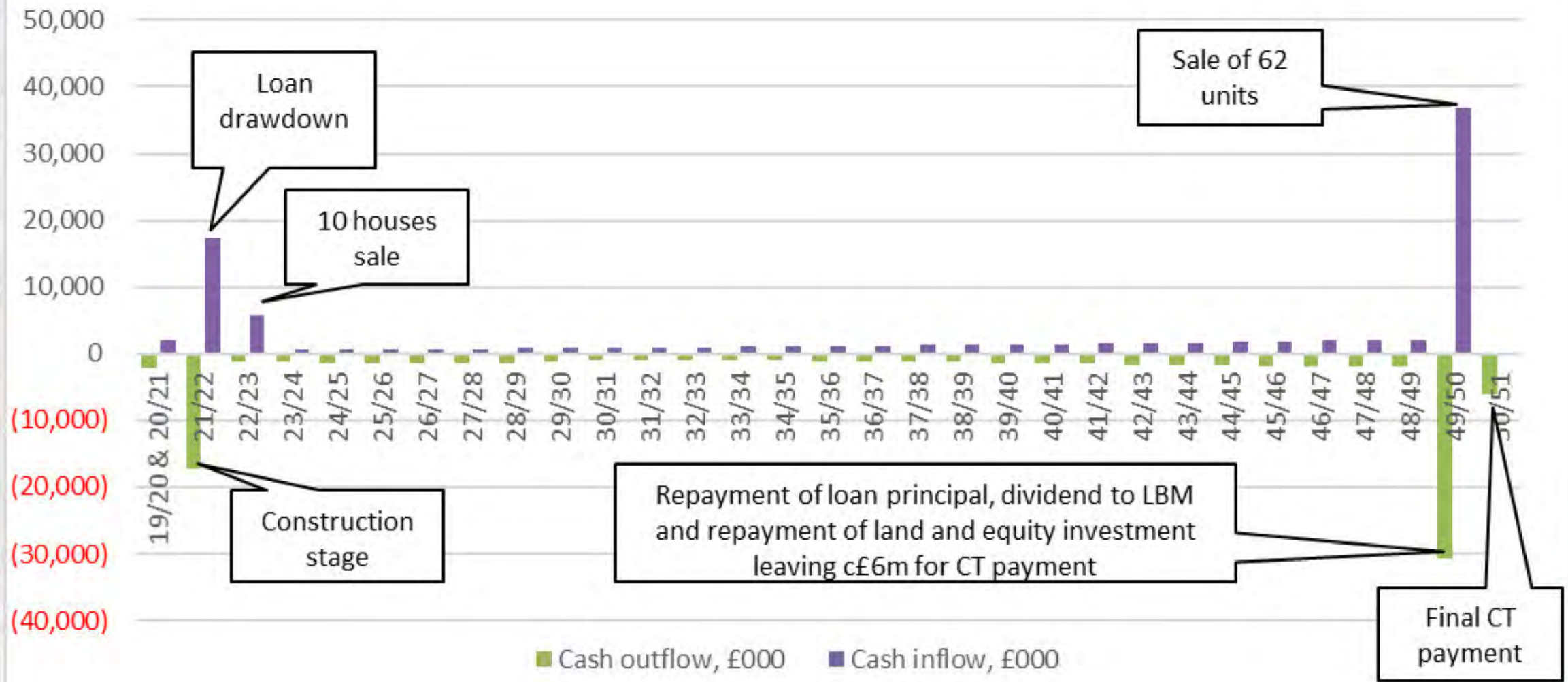
- Changes in the inputs affecting the project over its lifetime have the most significant effect on the project profitability
- Adverse variations in short term variables like house price of 10 houses on sale after construction have relatively small effect and can be disregarded
- Any combination of adverse variations in the above factors will have even greater effect on the project profitability



2020 MODEL CASH FLOWS

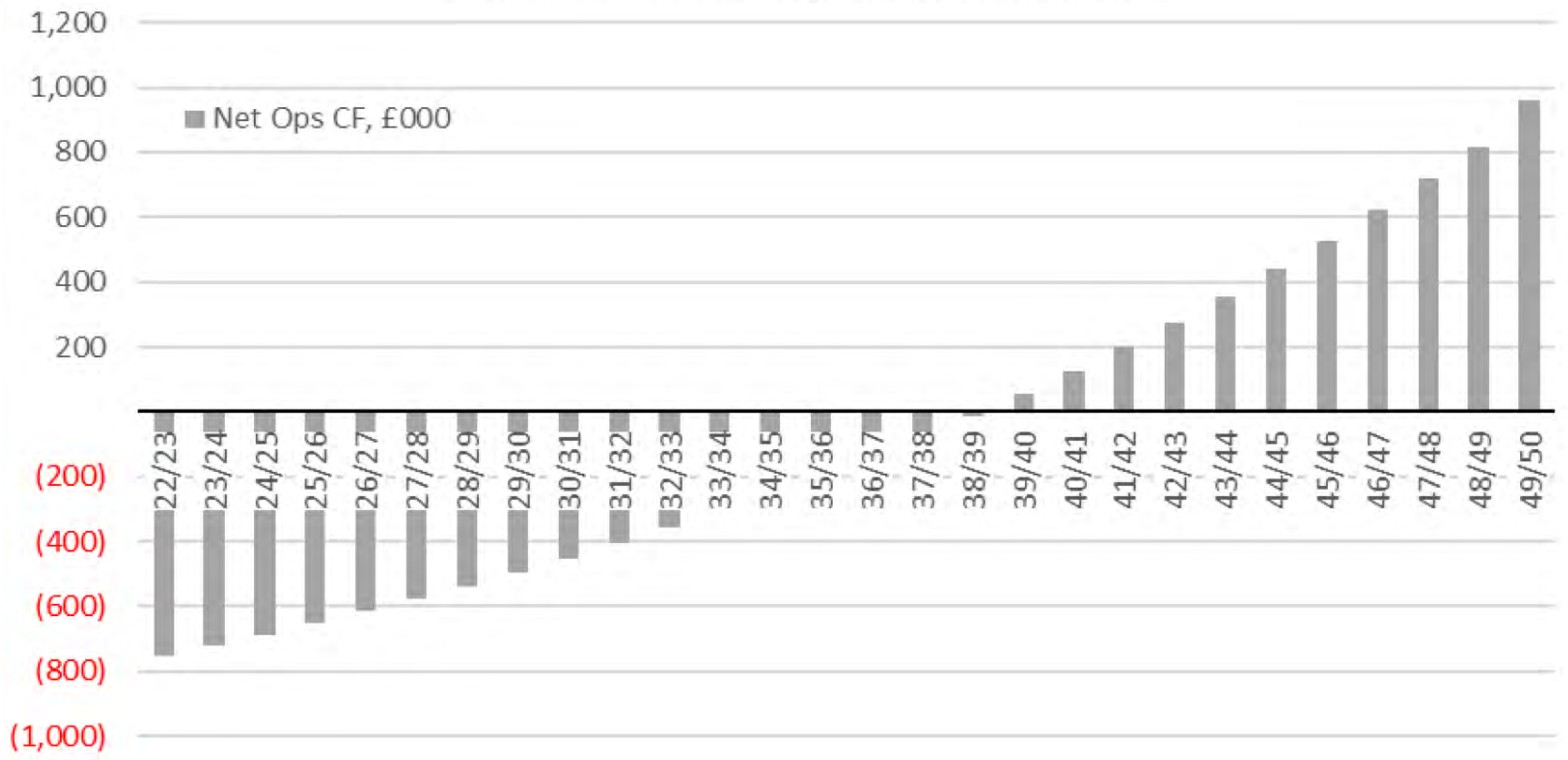
Cash flow over project timeline, £000

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2020 MODEL CASH FLOWS – Operating CF less annuity loan repayment

Net Operational Cash Flow, £000





CONCLUSIONS



Conclusions

- Costs have increased over the original Business Case
- A 2.94% return over 30 years is very low and represents a poor and risky return and is half the original expected return.
- MDL will not be in a position to repay full interest owed until year 17
- Full loan will not be repaid until 2049/50 on sale of units
- PWLB interest rates have been arbitrarily increased by 1% in part to counter speculative investments by Council's.
- Challenges in making accurate assumptions over the 30 year period (eg. Annual rents to increase by 4.3%).
- LBM risk appetite has reduced following significant budget constraints, impact of Covid and experience of Councils like Croydon.
- The Board are recommending jumping off at this stage.
- This was one of the key decision points included in the original Business Case.



Conclusion

Nov 2020: Currently at Key Jump off point 1.

MDL Board recommendation – not to proceed “Jump off point 1 exercised”

Recommend Option 2 (from slide 9)

Selling LBM land with MDL planning permission

- Utilisation of planning permission value added
- Disposing of idle land plots
- Value extraction at current asset state
- Risk: finding a potential buyer

Timeline: Formal report to MDL sub-committee pre-xmas.



