# Review of Northern Ireland Housing Associations' Reserves

## Prepared for the Assembly Research and Library Service

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PRICEWATERHOUSECOOPERS

Corporate Finance

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# Section 1

# Executive Summary

This document has been prepared solely for the addressees of the Engagement Contract under its terms and for no other person or purpose

# Executive Summary

- We were tasked with investigating the current level of reserves of the NI Housing Associations and how they are using these in financing their activities. We were also tasked with measuring the debt levels of the Associations and reviewing their asset management practices.
- We obtained the most recent filed accounts for each Association, as well as those for a sample of housing associations in GB ("Great Britain") which we used as a benchmark. We also sent a questionnaire to each NI Association to confirm our data, and collect further information.

We found that:

**Reserves**

- Of the £210 million held in reserves by the NI Associations in 2008/09, £208 million were Revenue Reserves. On average, each Housing Association had Revenue Reserves of just under £7,000 per unit, which compares to around £4,000 per unit for our GB sample.
- However, we are keen to emphasise the difference between reserves and cash. For example high reserves does not, per se, guarantee the ability to build additional houses now or fund major repairs in the future. Therefore we recommend carrying out a review of each Association's medium/long term cash flow projections to establish its ability to build additional units and cover future repairs.

**Asset Management**

- NI Associations increased their housing stock by 28% during the last five years. However many Housing Associations have experienced differing activity levels. The vast majority of NI Associations acquire new properties by self-building. Also, only a tiny proportion of the NI Associations' stock was disposed of last year- and mostly via the House Sales Scheme.
- NI asset management practices did not appear to be materially different from GB associations, although the latter have more diversified business models.

**Net Debt**

- The total net debt position of the Associations increased from £116 million to £246.6 million over the period 2006/07 to 2008/09. Similarly Gearing (defined as Net Debt / Property Net Book Value) has risen from 7.7% to 12.3% and the Debt / EBITDA (Earnings before Interest, Tax, Depreciation and Amortisation) measure has increased from 4.6x to 7.6x over this period. The net debt for those Associations that completed our questionnaire increased by 18% since the end of the 2008/09 period.
- In contrast, the debt levels for GB Associations are notably higher, with a current overall gearing in GB of 43% (19.7x Debt / EBITDA).

| ***2008/09 Accounts*** | **NI** | **GB** |
|---|---|---|
| **Total net debt** | £246.6m | £6,435.9m |
| **Gearing** | 12.3% | 43.0% |
| **Debt / EBITDA** | 7.6 x | 19.7 x |

**Stimulating Social House Building in NI**

In our view, the key options for stimulating social house building in NI are to:

- Continue to improve Associations' procurement efficiency;
- Use future HAG funding to enable the Associations, working together, to borrow funds now to build;
- Optimise the cash flows of the Associations in aggregate through suitable consolidation within the sector; and
- Investigate non-Housing Association led options. This could involve private sector solutions - through bringing in institutional investors or seed-funding an NI-focused Real Estate Investment Trust - or changing the status of the Northern Ireland Housing Executive to enable it to borrow to build houses.

# Section 2

# Objectives of this Review

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# Objectives of this Review

- There are currently 33 Housing Associations registered with the Department for Social Development ("DSD") in Northern Ireland ("NI"). These organisations, with the exception of Northern Ireland Co-Ownership Housing Association ("NICHA"), are listed in the table to the right.
- Between them, the Associations own and manage over 30,000 units – around a quarter of all the social housing units in NI – comprising self-contained units, bed spaces and supported units. This number continues to rise with over 1,800 new units having been started during the year to March 2010.
- As part of this review of sources of funding to enable the construction of more social housing in NI, it is being considered whether the reserves of inactive Housing Associations could be used to fund such additional social housing.
- Our report objectives are:
  - To identify the key types of reserves held by Housing Associations, how the levels of these reserves are being determined, and how they are being used;
  - Establishing the amount of these reserves and benchmarking this against the levels of reserves held by their GB peers;
  - To identify the new build activity of NI's Housing Associations and understand asset management practices in NI compared to those of housing associations in GB.
  - To consider the debt (or cash) levels of Housing Associations in NI as a comparison to those in GB; and
  - To consider, at a very high level, the options for encouraging Housing Associations or other current or potential future members of the social housing sector to build more social housing units.

**TABLE 1 :** NI Housing Associations, ranked by units, end 08/09

| | NI Housing Associations by number of units (08/09) | units |
|---|---|---|
| 1 | Helm Housing Ltd (BIH prior to 09/10) | 4,733 |
| 2 | FOLD Housing Association Ltd | 4,530 |
| 3 | Oaklee Housing Association Ltd | 4,147 |
| 4 | North & West Housing Association Ltd | 2,747 |
| 5 | Clanmil Housing Association Ltd | 1,992 |
| 6 | Habinteg Housing Association (Ulster) Ltd | 1,893 |
| 7 | SHAC | 987 |
| 8 | Alpha Housing Association (Presbyterian 05/06) | 946 |
| | **NI Housing Associations by number of units (08/09)** | **units** |
| 9 | Trinity Housing (Corinthinan 05/06; Choice 06/07) | 853 |
| 10 | Ulidia Housing Association Ltd | 845 |
| 11 | South Ulster Housing Association Ltd | 813 |
| 12 | Belfast Community HA Ltd | 595 |
| 13 | Woodvale & Shankill Housing Association Ltd | 473 |
| 14 | Newington Housing Association Ltd | 452 |
| 15 | Triangle Housing Association Ltd | 436 |
| 16 | Filor Housing Association Ltd | 400 |
| | **NI Housing Associations by number of units (08/09)** | **units** |
| 17 | Dungannon & District Housing Association Ltd | 392 |
| 18 | Flax Housing Association Ltd | 388 |
| 19 | Connswater Homes Ltd | 384 |
| 20 | Rural Housing Association Ltd | 384 |
| 21 | Open Door Housing Association (NI) Ltd | 341 |
| 22 | Craigowen Housing Association Ltd | 323 |
| 23 | Ark Housing Association (NI) Ltd | 280 |
| 24 | Ballynafeigh Housing Association | 250 |
| | **NI Housing Associations by number of units (08/09)** | **units** |
| 25 | Gosford Housing Association (Armagh) Ltd (incl Donacloney) | 203 |
| 26 | Grove Housing Association Ltd | 196 |
| 27 | St Matthew's Housing Association Ltd (incl. Clonard) | 178 |
| 28 | Abbeyfield UK (NI) Ltd | 164 |
| 29 | Wesley Housing Association Ltd | 144 |
| 30 | Hearth Housing Association Ltd | 93 |
| 31 | Broadway Housing Association Ltd | 84 |
| 32 | Covenanter Residential Association Ltd | 42 |

# Our Methodology

- In order to provide the most relevant and up-to-date information possible, we have used the most recent set of financial accounts submitted by each Housing Association to the Department of Enterprise, Trade and Investment (DETI). These accounts were for the years ended 31 December 2008 and 31 March 2009 depending on the respective reporting period of each Housing Association. Through discussion with DSD representatives it was concluded that more recent management accounts would not be used, as many of the selected Housing Associations may not produce these due to lack of accounting resources, and where such management accounts have been prepared, they may not be comparable to statutory audited accounts.
- However, a questionnaire generated by PwC, which contained a number of questions relating to financial information as at 31 March 2010, was issued to each of the Housing Associations. This questionnaire is provided in Appendix 1. At the 4th May 2010, we had achieved a response rate of 53%.
- The level of activity of each NI Housing Association has been assessed on the basis of the number of new unit starts during the past five years. This information has been provided by the DSD for the purpose of this report (and confirmed by us by our questionnaire). Having reviewed the scale and activity of the Housing Associations, it was noted that while there was a general correlation between size and activity (i.e. the larger Associations tended to be more active in building their estates) there were considerable exceptions to this pattern. We therefore decided to extend our review to include all NI's Associations. Given these inconsistencies, it was concluded that, notwithstanding the Committee's focus on inactive and larger Associations, a review of all of the Housing Associations would be more appropriate for the purpose of this report.
- This said, upon review of the activities of NI's Associations, we chose to exclude one from our review:

*Northern Ireland Co-Ownership Housing Association ("NICHA")*

NICHA operates NI's key shared ownership housing scheme. As such, its rental, management and repairing, and asset management models are substantially different from the rest of the NI Housing Associations. As such, NICHA has been excluded from the review.

- To put the findings of our review in perspective, we benchmarked the data of the NI Housing Associations against their counterparts in GB. The GB associations were chosen on the basis of size, measured by the number of units owned. From the top 10 associations, Anchor Trust was excluded as its primary activity is residential care. The 11th largest association has been selected in its place. The 10 housing associations selected therefore were:

**TABLE 2 :** GB housing associations benchmark 2009

| Housing Associations | No of units |
|---|---|
| L&Q Housing Trust | 47,082 |
| Home Group Limited | 42,185 |
| Places for People Homes | 35,380 |
| Wakefield and District Housing Ltd | 30,883 |
| Gentoo Sunderland Limited | 29,391 |
| Sanctuary Housing Association | 29,371 |
| Midland Heart Limited | 26,169 |
| The Guinness Trust | 21,216 |
| Incommunities Limited (Bradford) | 21,101 |
| William Sutton Housing Association Ltd | 20,475 |

Source: Tenants Service Authority

- Some of the above entities, however, engage heavily in activities other than general needs social housing. Where possible, we have used only the metrics of the social housing operation.

# Section 3

# Analysis of NI Housing Associations' Reserves

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# What are reserves and why do housing associations have them?

**What are reserves?**

- When a housing association generates more income than it spends, a reserve is created.

**Different types of reserves**

- There are four types of reserves which housing associations maintain:
  - Capital Reserves;
  - Designated Reserves;
  - Restricted Reserves; and
  - Accumulated Surpluses.
- The last 3 reserve types, above, together comprise the Revenue Reserves and are by far the largest reserves in most housing associations.

**Capital Reserves**

- Capital Reserves comprise revaluation reserves, which represent the extent to which the most recent valuation of assets exceeds their historical cost. The majority of these reserves arise when a housing association adopts an accounting policy of including its property assets at a valuation in the balance sheet. Most housing associations have not adopted such a policy, preferring to include their property assets in the accounts at historical cost. An important feature of this reserve is that it does not derive from the generation of cash surpluses and so is referred to as a 'Capital Reserve'. Revaluation reserves can only be realised as cash on the disposal of property assets.

**Designated Reserves**

- Designated Reserves represent surpluses which have been earmarked by the Association's board for a particular purpose.
- They often include major repairs, cyclical repairs and maintenance, and welfare funds. Designation seeks to help the users of the accounts identify the extent to which Housing Associations have specific future commitments or obligations to fulfil. Associations are free to designate or un-designate reserves as they wish.
- The DSD provides guidance on the level of reserves a Housing Association should put aside – for example, it is suggested by the Department that provisions should be made annually as follows:

  *New Build* – 0.8% of the approved works cost, minimum £525.

  *Rehabilitation / ESP* – 1% of the approved works, minimum £590.
- Our survey found a mixed level of adoption of DSD guidelines.

**Restricted Reserves**

- Restricted Reserves represent surpluses which can only be used in accordance with the wishes of funders, regulatory bodies, or other external bodies (e.g. banks). This reserve is a relatively new feature for NI Associations' Balance Sheets.

**Accumulated Surpluses**

- This reserve represents an accumulation of retained surpluses which have been generated by a housing association from its annual operating activity. They represent the difference between total income received and total expenditure incurred, after making transfers to specific reserves, e.g. Designated or Restricted Reserves. Sometimes they are referred to as 'free reserves' to recognise that there are no specific restrictions on how they may be used.
- If a housing association could distribute its assets, as a company limited by shares can, it could pay these out to the level of its Accumulated Surpluses, subject to availability of cash. We believe that most of NI's Associations are Industrial & Provident Societies, so cannot distribute their reserves; however this goes beyond the scope of our report, so needs further confirmation.

# What are reserves and why do housing associations have them?

**Why are reserves necessary?**

- Securing the future viability of the association is essential. The way the sector has chosen to do this is by setting aside some of its current income as a 'reserve' against future costs or uncertainties. This is intended to enable the housing associations to provide reliable services and funding over the longer term. They will be able to absorb setbacks and take advantage of change and opportunity.
- The level of reserve an association needs to hold can only be determined by a realistic assessment of each organisation's own funding needs. This assessment should consider the future financial obligations faced by the association.
- Housing associations have a range of financial obligations in the running of their organisation on a day-to-day basis. They also have to prepare for, and fund, future obligations.
- The DSD identifies the following reasons for generating and maintaining reserves in its Housing Association Guide:

  ***Internal Subsidy***

  An association often establishes reserves where it wants to set aside funds to expand its activities or exploit new areas of opportunity. In the past, this has also included the financing of property assets not covered by grant or loan, as well as an association's investment in office premises.

  ***Future Major Repairs***

  As stock ages, the volume of repair work generally increases. An element of each year's surplus needs to be set aside to meet this expenditure. Under the Accounting Code of Practice the amount set aside for major repairs must be separately identified in a designated fund. The remaining financial obligations (detailed below) need to be met from the association's 'general reserves.'

***Management of Risk***

The past is an unreliable guide to the future. Many financial and economic factors are outside the control of a housing association. Surpluses may therefore contain short term benefits which may not continue in future years. Judgements have to be made about the likely extent of future adverse circumstances. It is better to generate a reasonable level of surplus each year than to seek a large rent increase (if even available) if risks were to crystallise. This is becoming an even more critical area in a period of constant change in political, economical and environmental terms.

***Capital Loan Repayment***

Part of the surplus made each year represents monies required to repay loans and, according to the latest available accounts, NI Associations now have over £300 million of loans and overdrafts outstanding. While it may be possible to extend the obligation to repay loans over a longer time frame, at some point loan capital has to be repaid. Indeed, lenders as a matter of course impose loan covenants upon housing associations which require them to achieve a certain level of surplus. This is intended to provide comfort to lenders that associations will not default on loans.

***Working Capital***

This is the amount of funds needed to pay debts as they become due and to finance stocks and debtors. An element of the reserves needs to be held to ensure an appropriate cash position to meet on-going operational needs.

Notwithstanding the above detailed guidance for creating and maintaining reserves, we found inconsistencies across the Housing Associations in the way they charge reserves.

# How useful are reserves as a measure?

**Reserves as indicators of financial health**

- For housing associations to ensure they are able to meet their objects (principally, the provision of social housing) sustainably, it is necessary for them to not only cover their cash costs as they arise, but to ensure that they will be able to continue to do this in the medium term.
- Charging amounts to the Income & Expenditure account for the future costs of the association (i.e. establishing reserves), is a helpful discipline for recognising that often the future costs and cash outflows of an association are higher than today's costs. However, there is a danger that in "conservatively" apportioning amounts to a reserve, a housing association board could be unknowingly under-providing for its future cash needs.
- For, while the charging of reserves is viewed by some boards as "putting aside money for a rainy day", most housing associations do not maintain these reserves as cash balances, but merely as accounting entries; instead cash surpluses are often re-invested, long-term into new properties.
- Of critical importance, then, is that housing associations ensure that they can generate sufficient cash to meet their future liabilities as they fall due, irrespective of their policy on accounting reserves.
- Boards need to ensure that a housing association's financial strategy provides for sufficient cash to be available to perform future major repairs when required (based on robust assessments of the needs of the stock) – and indeed to meet all operating costs.
- The converse, of course, is true – over time, rent levels are likely to rise and increased housing stock, from investing cash "reserves", will result in yet more rental income and, all else being equal, more capital receipts from more sales under the House Sales Scheme.
- The foremost method of ensuring sufficient resources will be available to meet financial obligations as they become due is maintaining medium and long term cash flow forecasts, which extend through cyclical and major repair cycles.
- Feedback from our questionnaire has indicated that cash flow projections **are** being produced by the NI Housing Associations – but often on a 1-3 year period for operations or up to 25 years for new capital investment projects. While we understand the reasons for these two time horizons for short term budgeting and long-term planning, we believe that, rather than just for project plans, each association should have medium-term (10 years+) cash flow projections in place for their entire organisation (to ensure funding will be in place to meet the association's overall debt repayments, major repairs and other ongoing costs). We understand that confirming proper corporate governance and business planning is part of the DSD's annual inspection process, but we would like to ensure that their process – or another independent review – confirms that NI's Associations have a suitable cash flow plan for meeting their needs in the short, medium and long term.
- Several Associations, including Clanmil, have recently invested in an MIS package, Brixx, which, we understand, supports good quality long-term cash flow forecasting. Other Associations should consider investing in this or similar packages.
- A review of the Associations' medium-term cash flow projections would also uncover the capacity of each Association to undertake additional house building.

# Level of Reserves in NI Housing Associations

- Table 3 shows the level of reserves of NI’s Housing Associations (excluding NICHA, as previously explained) during the period 2006/07 to 2008/09, analysed by reserve type.
- In 2008/09, total NI Housing Association reserves were £210 million, of which £208 million were Revenue Reserves and £2 million were Capital Reserves.
- It can be seen that both the largest reserves – the Accumulated Surpluses and the Designated Reserves - have increased consistently over the last 3 years.
- On average, each Housing Association had revenue reserves of just under £7,000 per unit.
- The £7,000 per unit for the NI Associations compares to an amount in excess of £4,000 per unit for our GB sample. It should be noted, however, that our review of the GB housing associations has revealed that there is little or no emphasis on Designated Reserves in these organisations. In fact, only two of the 10 GB associations reviewed had separately-identified Designated Reserves.

**TABLE 3 :** NI Housing Associations’ Reserves

| NI HA | 2006/07 £'000 | 2007/08 £'000 | 2008/09 £'000 |
|---|---|---|---|
| **Revenue Reserves** | | | |
| Accumulated surpluses | 94,847 | 103,933 | 112,323 |
| % Change | | 9% | 7% |
| Designated reserves | 73,318 | 80,784 | 89,435 |
| % Change | | 9% | 10% |
| Restricted reserves | n/a* | | 4,919 |
| % Change | | n/a | |
| Other designated reserves | 6,163 | 8,791 | 1,190 |
| % Change | | 30% | -639% |
| Total Revenue Reserves | 174,328 | 193,508 | 207,867 |
| % Change | | 10% | 7% |
| **Capital Reserves** | | | |
| Revaluation | 2,338 | 2,426 | 2,171 |
| % Change | | 4% | -12% |
| **Total All Reserves** | 176,666 | 195,934 | 210,038 |
| % Change | | 10% | 7% |

* Restricted reserves were not provided for in 07/08 or 06/07

# Section 4

# NI Housing Associations’ activity levels / Asset Management practices

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# Levels of Activity in NI

- As at 31 March 2009, the number of social housing units owned by registered Housing Associations in Northern Ireland was 30,688. During the year to end March 2010, NI Housing Associations started construction on 1,838 new units, exceeding the Minister’s target of 1,750 starts during the same period. This was a significant increase in starts from the prior year. Including new starts, this figure then is likely to have increased to more than 32,000 as at 31 March 2010. The growth in the total housing stock is illustrated in Chart 1.
- Chart 2 illustrates the number of starts from 2005/06 to 2009/10. During this period, there were 7,120 starts of which 4,650 were undertaken by five Housing Associations, some 65% of the total.
- For the purpose of this report, activity has been measured in terms of the number of starts during 2005/06 to 2009/10 expressed as a percentage of housing stock as at the end of 2004/05. Overall, NI Housing Associations have experienced a 28% increase in housing stock (ignoring existing property purchases and disposals) during the last five years.
- The level of activity by Association during this period has varied significantly with the five most active Housing Associations seeing an average increase of 50% during the period under review. This compares to an increase of less than 1% for the five least active Associations during the same period.

**CHART 1 :** Total units owned by the NI Housing Associations

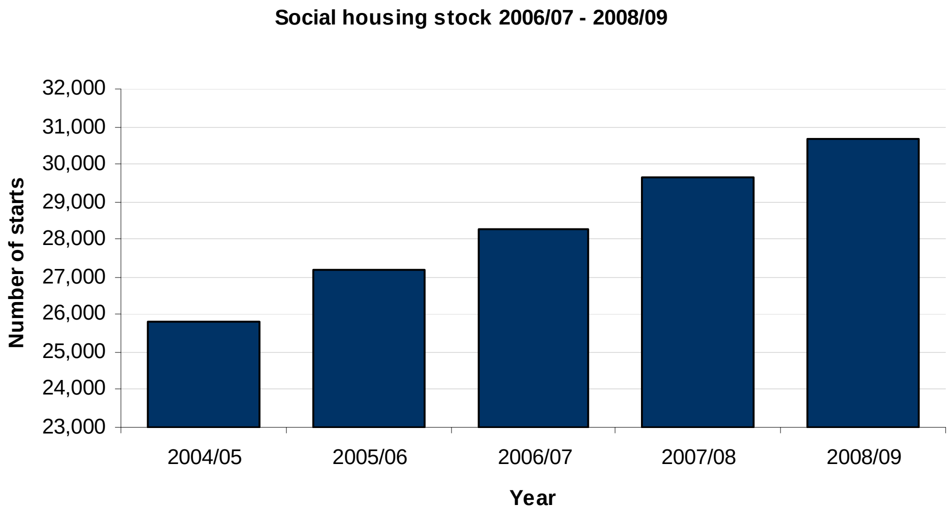
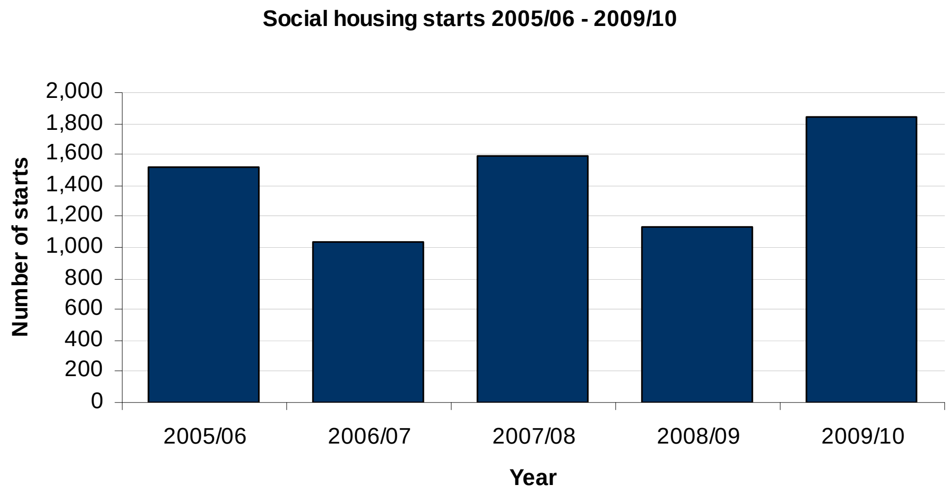



**CHART 2** : Total New-build starts for the NI Housing Associations



# Levels of Activity in NI

- Table 4 shows the activity of each of the NI Housing Associations over the past five years, (measured as a % of units added in the last 5 years divided by the opening stock 5 years ago), including the number of unit starts during this period.
- Interestingly, only 3 of the 8 largest Housing Associations (measured by number of units) are included in the most active table, being Trinity Housing, Clanmil Housing Association and Ulidia Housing Association.
- On the other hand, most of the least active Housing Associations are also the smallest in NI, with the notable exception being SHAC which is in fact the 7th largest.

**TABLE 4 :** Total units owned by the NI Housing Associations

| Most Active | | starts | % increase |
|---|---|---|---|
| **1** | Connswater Homes Ltd | 228 | 81% |
| **2** | Trinity Housing (Corinthinan 05/06; Choice 06/07) | 373 | 59% |
| **3** | Clanmil Housing Association Ltd | 897 | 59% |
| **4** | Dungannon & District Housing Association Ltd | 131 | 45% |
| **5** | Belfast Community HA Ltd | 188 | 44% |
| **6** | Ulidia Housing Association Ltd | 243 | 42% |
| **7** | Triangle Housing Association Ltd | 146 | 38% |
| **8** | Wesley Housing Association Ltd | 49 | 36% |

| Moderately Active | | starts | % increase |
|---|---|---|---|
| **9** | North & West Housing Association Ltd | 788 | 34% |
| **10** | Flax Housing Association Ltd | 94 | 33% |
| **11** | Hearth Housing Association Ltd | 30 | 32% |
| **12** | South Ulster Housing Association Ltd | 216 | 31% |
| **13** | Habinteg Housing Association (Ulster) Ltd | 453 | 29% |
| **14** | FOLD Housing Association Ltd | 1,045 | 28% |
| **15** | Rural Housing Association Ltd | 88 | 27% |
| **16** | Helm Housing Ltd (BIH prior to 09/10) | 1,060 | 27% |

| Least Active | | starts | % increase |
|---|---|---|---|
| **17** | Oaklee Housing Association Ltd | 850 | 23% |
| **18** | St Matthew's Housing Association Ltd (incl. Clonard) | 30 | 23% |
| **19** | Grove Housing Association Ltd | 27 | 15% |
| **20** | Ark Housing Association (NI) Ltd | 41 | 12% |
| **21** | Filor Housing Association Ltd | 27 | 8% |
| **22** | Woodvale & Shankill Housing Association Ltd | 32 | 7% |
| **23** | Newington Housing Association Ltd | 27 | 7% |
| **24** | Abbeyfield UK (NI) Ltd | 11 | 6% |

| Not Active | | starts | % increase |
|---|---|---|---|
| **25** | Ballynafeigh Housing Association | 14 | 6% |
| **26** | Gosford Housing Association (Armagh) Ltd (incl Donacloney) | 6 | 3% |
| **27** | SHAC | 14 | 1% |
| **28** | Alpha Housing Association (Presbyterian 05/06) | 12 | 1% |
| **29** | Open Door Housing Association (NI) Ltd | 0 | 0% |
| **30** | Craigowen Housing Association Ltd | 0 | 0% |
| **31** | Covenanter Residential Association Ltd | 0 | 0% |
| **32** | Broadway Housing Association Ltd | 0 | 0% |

# Asset Management Practices - NI

***Additions***

- As illustrated earlier, the overall housing stock owned and managed by Housing Associations in NI has grown significantly during the past five years.
- The DSD has set out rigorous guidance on procurement, (which conforms with EU Procurement Directives), for Housing Associations who wish to avail of funding in the form of Housing Association Grants ("HAG"). In addition, procurement has been streamlined by virtue of the establishment of the Housing Association procurement groups (APEX, ABACUS, ACCORD and PREMIER), allowing for greater efficiencies.
- The requirement for new housing stock in NI is generally satisfied through the procurement of new built stock (1,838 units in 2009/10). Indeed of the new units added by the Housing Associations this year, more than 90% of our survey sample were self-built. (However a number of larger, more active Associations who might be more likely to make some acquisitions didn't complete the questionnaire).
- With the aid of Existing Satisfactory Purchase (ESP) grants, distressed part-developed properties have also been acquired recently and brought up to a habitable state by a small number of Housing Associations for the provision of social housing.

***Stock/ Maintenance***

- At present, the most common property type held by Housing Associations in NI are self contained units comprising:
  - 1 bed / bedsit (35% of stock)
  - 2 bed (25% of stock)
  - 3 bed (22% of stock)
- Only 3% of stock has 4 bedrooms or more. The remaining stock (15%) is bedspaces primarily within special needs units. It has been indicated by DSD that one bed units are no longer being built with the current emphasis being on two and three bed units.
- With the notable exception of Hearth Housing Association, which primarily, but not exclusively, provides social housing for rent in restored historic buildings, the majority of housing stock owned by Associations in NI is less than 25 years old.
- The Associations are expected to undertake maintenance on their stock to ensure that the Decent Homes Standards are met at all times. However the Associations are self-regulating on this front and there are no formal stock condition reports produced by most. It is not clear, therefore, that the Decent Homes Standard is being consistently achieved – although it should be noted that while the associations in GB would claim to be meeting this target, there is a view that they starting to fall short.
- Also there have been no wholesale scheme sales (other than several small re-assignments of schemes from one association to another, pre-completion).

***Disposals***

- Our questionnaire confirmed that c 1% of housing stock was disposed of during the past year, almost all of which were via the House Sales Scheme, with a tiny proportion by way of demolition Also, one Association has vested three properties with NIHE.
- Because the properties in urban locations in Northern Ireland are relatively new, the Associations have generally not been involved in any extensive regeneration projects.

# Asset Management Practices - GB

- GB housing association asset management practices appear generally more active than their NI counterparts, partly due to their support of diverse UK government housing policies.
- Notting Hill Housing Trust’s “Asset Management Strategy for 2006-2011” is reflective of the strategies across a number of the GB associations. It can be summarised as follows:
  - New build construction to cater for new needs and to replace obsolete or uneconomic stock;
  - Acquisition of property, by purchase, development or transfer from other landlords to maintain a balanced portfolio, address newly emerging needs and achieve economies of scale in the management;
  - Refurbishment and remodelling of dwellings to ensure they remain attractive, meet modern requirements and tenant expectations;
  - A planned maintenance programme, achieving economies by replacing components just before they would otherwise require response repairs, anticipating changes in minimum acceptable standards, and reducing future requirements for cyclical maintenance;
  - Cyclical maintenance to prevent deterioration in the physical condition of the stock;
  - A responsive maintenance service, to ensure that residents remain satisfied with their accommodation and to prevent unplanned deterioration in its condition;
  - An efficient and effective voids repair service, helping to speed the repairs process and protect the association’s revenue; and
  - Sales and or swap of property, to remove liabilities or to generate funds for future re-investment.
- In addition to the more active management of asset disposals, the principal other contrasting component of asset management practices of housing associations in GB compared to those in NI, is their level of activity relating to regeneration projects.
- Almost all of GB’s largest social housing groups have diversified rapidly over the past number of years, becoming multi-faceted businesses with activities including health and social care, and significant mixed tenure offerings (i.e. including private rental).
- It has been noted from discussions with relevant NI stakeholders that some of the business models adopted by GB housing associations, such as those which have incorporated mixed tenure in developments, have not always been entirely successful. However, many associations are now keenly aware that it was this sort of growth that brought about the demise of Ujima Housing Association, Britain's oldest and largest black Housing Association, in 2008. While the diversification policy in GB has been promoted by government, it may be viewed that a different (simple) model, as is employed in NI, also has many positive attributes.

# Section 5

# Analysis of NI Housing Associations' Debt Levels

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# Current Debt Levels

### Northern Ireland Housing Associations' Debt

- Ensuring that it has sufficient liquid funds (or access to these funds as needed) is a fundamental requirement for each of NI's Housing Associations, in pursuing its (charitable) objects.
- As at 31 March 2009, loans and overdrafts owed by NI Housing Associations in 2008/09 totalled £307 million, with cash balances totalling £60 million. Net debt (loans and overdrafts, less cash and current asset investments) therefore totalled £247 million. This compares with £175 million in 2007/08 and £116 million in 2006/07.
- The net debt for those Associations who completed our questionnaire has since increased by £34 million (an uplift of 18% of the net debt of those Associations).
- Measuring net debt as a percentage of the depreciated cost of housing properties (before deduction of HAG), total gearing of the NI Housing Associations sat at 12.3% in 2008/09.
- There has been a noted increase in this gearing ratio over the past three years with the ratio for all NI Housing Associations rising from 8% in 2006/07 to 10% in 2007/08.
- The other key indication of the level of indebtedness for a housing association, is its ability to service its debt obligations with earnings and cash flow. While the housing association sector often quotes EBITDA/interest cost as its measure of debt serviceability, because interest rates are at an historic low and will almost certainly rise over the next 3 years, we prefer the Debt/EBITDA ratio to establish how well the HAs are positioned to meet their loan obligations (as do the main lenders to the NI Housing Associations).

**TABLE 5**: Total Net Debt for NI's Housing Associations

| | 2006/07 actual | 2007/08 actual | 2008/09 actual |
|---|---|---|---|
| **Total net debt** | £116.2m | £175.5m | £246.6m |
| **Net debt per unit** | £4,271 | £6,209 | £8,036 |
| **Gearing** | 7.7% | 9.9% | 12.3% |
| *Range - low* | *net cash* | *net cash* | *net cash* |
| *Range - high* | *30.6%* | *32.7%* | *47.6%* |
| **Debt / EBITDA** | 4.6 x | 5.6 x | 7.6 x |

- We calculated the Housing Associations' Debt/EBITDA using earnings or EBITDA, comprised of the Operating Surplus before exceptional items, depreciation on owned tangible fixed assets, property impairment, amortisation of grants and contributions, amortisation of negative goodwill, movement in service charges equalisation account, FRS 17 non-cash pension charge / (gain), interest payable and profit on disposal of fixed assets.
- For NI Associations, as a whole, Debt/EBITDA was 7.6x at 31 March 2009.
- A summary of the debt levels and ratios during the past 3 years is shown in Table 5.

# Current Debt Levels

- Table 6 shows the debt of each Association (£m), as a proportion of its Net Book Value of Property (Gearing %) and as a multiple of its latest EBITDA.
- The average gearing level, measured on the same basis, shows a range from "net cash" to 48% gearing; similarly, the Debt/EBITDA multiple ranged from a negative multiple (where there was net cash and positive EBITDA) to 66.8x EBITDA.
- In particular, on the measure of Debt/EBITDA, it should be noted that the results of Dungannon & District (22.8x) and those of Craigowen (66.8x) show particularly high Debt/EBITDA ratios. In the case of the former, high bank loans are held as against a low EBITDA, whereas in relation to the latter, high cash balances are held as against a negative EBITDA.
- It is also worth noting that Rural has a high level of gearing, second only to that of Dungannon; however its Debt/EBITDA measure is a reasonable degree better than Dungannon's.
- Furthermore, SHAC appears to be consistently loss-making over the period we have considered; however it is also consistently in a net cash position.

**Table 6** : Net Debt by association

| NI Housing Associations by number of units (08/09) | | units | Net Debt (£m) | Gearing % | Debt/EBITDA * |
|---|---|---|---|---|---|
| 1 | Helm Housing Ltd (BIH prior to 09/10) | 4,733 | 59,910 | 17% | 12.4 |
| 2 | FOLD Housing Association Ltd | 4,530 | 6,132 | 3% | 1.4 |
| 3 | Oaklee Housing Association Ltd | 4,147 | 37,849 | 16% | 11.5 |
| 4 | North & West Housing Association Ltd | 2,747 | 44,863 | 20% | 11.6 |
| 5 | Clanmil Housing Association Ltd | 1,992 | 17,771 | 10% | 5.8 |
| 6 | Habinteg Housing Association (Ulster) Ltd | 1,893 | 28,210 | 11% | 10.7 |
| 7 | SHAC | 987 | (382) | net cash | 2.5 |
| 8 | Alpha Housing Association (Presbyterian 05/06) | 946 | 1,512 | 3% | 6.4 |
| 9 | Trinity Housing (Corinthinan 05/06; Choice 06/07) | 853 | (1,039) | net cash | (1.5) |
| 10 | Ulidia Housing Association Ltd | 845 | 12 | 0% | 0.0 |
| 11 | South Ulster Housing Association Ltd | 813 | 13,096 | 25% | 9.8 |
| 12 | Belfast Community HA Ltd | 595 | 4,410 | 9% | 8.1 |
| 13 | Woodvale & Shankill Housing Association Ltd | 473 | (4,528) | net cash | (7.9) |
| 14 | Newington Housing Association Ltd | 452 | 1,821 | 6% | 4.3 |
| 15 | Triangle Housing Association Ltd | 436 | 1,379 | 5% | 3.4 |
| 16 | Filor Housing Association Ltd | 400 | 4,230 | 18% | 8.5 |
| 17 | Dungannon & District Housing Association Ltd | 392 | 14,960 | 48% | 22.8 |
| 18 | Flax Housing Association Ltd | 388 | 3,719 | 11% | 5.7 |
| 19 | Connswater Homes Ltd | 384 | 4,949 | 11% | 7.1 |
| 20 | Rural Housing Association Ltd | 384 | 10,163 | 30% | 14.9 |
| 21 | Open Door Housing Association (NI) Ltd | 341 | (1,772) | net cash | (17.2) |
| 22 | Craigowen Housing Association Ltd | 323 | (2,339) | net cash | 66.8 |
| 23 | Ark Housing Association (NI) Ltd | 280 | 1,237 | 7% | 4.0 |
| 24 | Ballynafeigh Housing Association | 250 | 738 | 5% | 2.6 |
| 25 | Gosford Housing Association (Armagh) Ltd (incl Donacloney) | 203 | 396 | 4% | 1.7 |
| 26 | Grove Housing Association Ltd | 196 | 2,565 | 19% | 9.4 |
| 27 | St Matthew's Housing Association Ltd (incl. Clonard) | 178 | (837) | net cash | (3.8) |
| 28 | Abbeyfield UK (NI) Ltd | 164 | (815) | net cash | (4.2) |
| 29 | Wesley Housing Association Ltd | 144 | (1,573) | net cash | (15.6) |
| 30 | Hearth Housing Association Ltd | 93 | 34 | 1% | 1.2 |
| 31 | Broadway Housing Association Ltd | 84 | (561) | net cash | (15.6) |
| 32 | Covenanter Residential Association Ltd | 42 | (178) | net cash | (7.1) |

* last reported

# Benchmarking

### GB housing associations' debt

- In contrast to their NI counterparts, the Debt/EBITDA ratios of the top ten housing associations in GB was 19.7x (versus 7.6x), and the gearing ratio was 43%, as at 31 March 2009.
- The markets now recognise that debt levels in the GB housing associations are high and the ability of housing associations in GB to raise new finance facilities remains challenging with substantial margins on interest charges and demanding covenants. Evidence gathered by the Tenants Service Authority, the social housing regulator in England, suggests that there has been a significant increase in associations raising finance through the capital markets as an alternative to traditional (bank) sources of finance. The same report, 'Quarterly survey of Housing Associations and review of 2009-10', stated that no association had reported anticipating a covenant breach in the coming 12 months.
- As a guide, the sector often looks for an EBITDA/interest cover of 1.2x as a minimum (and gearing of less than 50%). With an average current interest cost of, say, 3%, (being current Libor plus its average margin / spread on the GB associations' listed bonds) our GB associations sample would currently have an EBITDA/interest cover of nearly 1.7x.
- A report from Baroness Ford in 2007 highlighted that the Housing Association movement in NI could be more highly geared and since then the increase in total net debt, albeit modest, has been due to a downward movement in grant rates.

**TABLE 7**: Debt for NI and GB housing associations

| ***2008/09 Accounts*** | **NI** | **GB** |
|---|---|---|
| **Total net debt** | £246.6m | £6,435.9m |
| **Gearing** | 12.3% | 43.0% |
| **Debt / EBITDA** | 7.6 x | 19.7 x |

# Section 6

## Options for stimulating social house building in NI

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# Options for stimulating social house building in NI

**Housing Associations**

- The realistic bases on which government can encourage NI's Housing Associations to increase their level of new builds are :
  - with greater annual HAG funding from the DSD;
  - greater procurement efficiency;
  - optimising the cash flows of each of the Associations; or
  - restructuring the way / timing in which HAG is paid.

***Greater annual HAG stimulus***

An increase in the Social Housing Development Plan budget for new house building is likely to be very challenging in current government budget planning.

***Greater procurement efficiencies***

As set out on page 13, this is something that the DSD is already working on. We believe that co-ordinating the new build activity into 4 active groups presents a suitable platform for enabling active bidding for HAG. This will reduce the HAG required per new unit – thereby increasing the number of new units added (assuming a constant level of HAG);

***Optimising the cash flows of each of the Associations***

As discussed on page 7, on the basis of just reserves and conventional accounting data, we are unable to establish whether NI's Housing Associations are under-funded in relation to their future maintenance obligations, or over-funded and have the ability to build more housing.

However, a comprehensive review of the medium-term cash flows of each these Associations (plus discussions with their boards) would enable such a view to be taken.

Having established a view on each Housing Association's capacity to engage in further house building, the key pressures that DSD could apply to achieve this outcome would appear to be around HAG – suspending the Association's right to new HAG (although this, by definition, will not have the desired effect) or suspending its recycling (i.e. requiring the Association in question to repay any HAG attached to any units it sells). Beyond this, DSD would need to consider an appeal to boards to consider their charitable objects - for example Fold's first object is: "to carry on for the benefit of the community, the business of providing housing……" This is not atypical.

DSD should also consider financial incentives for the board and/or managers in NI's Housing Associations to maximise, the number of social housing units they manage on a long-term, sustainable ("decent") basis.

Also, DSD should consider whether they should undertake even further moves to consolidate the number of Associations (while devising mechanisms for retaining community identity), as a good financial manager is able to run a more efficient balance sheet/funding structure across a portfolio of assets under management – as opposed to a manager of a single scheme, who always need to finance his business conservatively just in case the unexpected happens. This is known as the insurance or portfolio approach to asset management.

***Restructuring the way / timing in which HAG is paid***

Working together, NI's Housing Associations could borrow now to fund an immediate social house building stimulus. Future HAG could then be used to repay this loan over the next, say, 20 years.

A number of economic commentators would support the short-term economic stimulus effect of this approach in the current climate, as well as its clear, positive, impact on current housing stress.

# Options for stimulating social house building in NI

**Non-Housing Association-led options**

PwC is currently working with DSD, the Northern Ireland Housing Executive ("NIHE") and the Strategic Investment Board ("SIB") to design a model for stimulating private social house building in NI. This could involve bringing in institutional investors from outside NI, or seed-funding an NI-focused Real Estate Investment Trust ("REIT"). This would supplement the Associations' house building programmes.

In addition to NI's Housing Associations and, potentially private sector landlords, the other key stakeholder in the social housing sector, with the capacity to add new social housing units, is the NIHE. However, its status/role would need to be changed to allow it to contribute significantly towards this goal.

# Appendix 1

## Questionnaire circulated to Housing Associations by PwC

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# Appendix 2

# Key Financial Data on NI Housing Associations

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