Great Places Housing Group

Business Plan 2021/22

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If you have any questions on the business plan, please contact Phil Elvy, Executive Director of Finance, at **phil.elvy@greatplaces.org.uk**

The information included within this report is for information purposes only. The Financial results quoted are unaudited. The report may contain forward looking statements and actual outcomes may differ materially. No statement in the report is intended to be a profit estimate or forecast. We do not undertake to revise such statements if our expectations change in response to events. This report does not constitute legal, tax, accounting or investment advice.

Executive Summary

1

The Great Places Housing Group Board is pleased to present its business plan for 2021/22 and beyond that maintains the financial strength and long-term viability of the Group. It also reflects the ambitions outlined in the new Corporate Plan.

This business plan has been developed during the UK's third Covid lockdown, taking into account the rollout of the vaccine programme which has allowed the Government to set out a roadmap to recovery. During the last 12 months the Group has coped well with both the operational and financial impact of the pandemic, establishing new ways of working for front line colleagues to accompany a working from home model for most other colleagues.

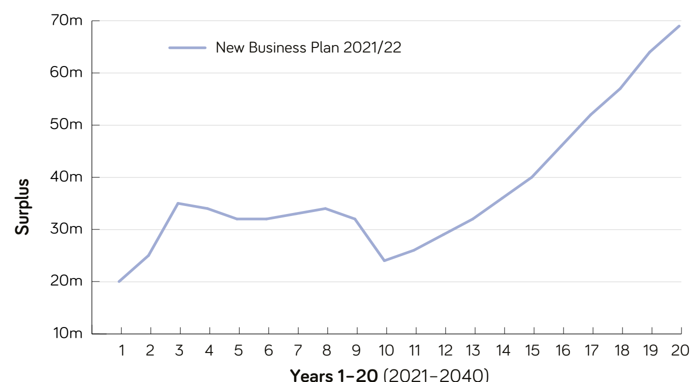
Key impacts have included periods of emergency or essential only repairs, delays to development, with a knock on impact on sales and deferral of investment works. Despite the pandemic, arrears and void re-let performance has remained strong with the furlough scheme and the temporary uplift to Universal Credit payments at least partially protecting many of our customers. The Group's Hardship Fund and Community Resilience Fund have also helped mitigate the effects of the pandemic. There is however a real risk of a further, more significant growth in unemployment as furlough is phased out.

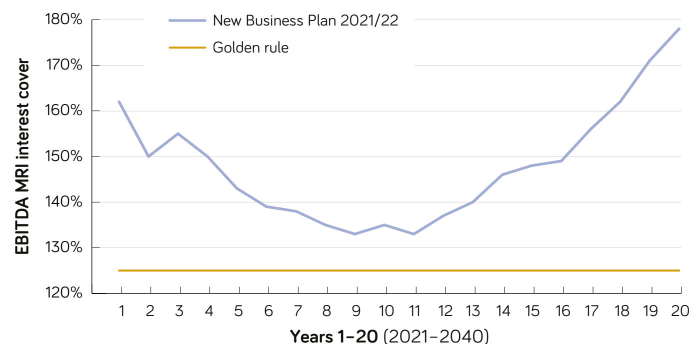
The plan incorporates our best understanding of any ongoing impact on the Group. This new and fully updated plan:

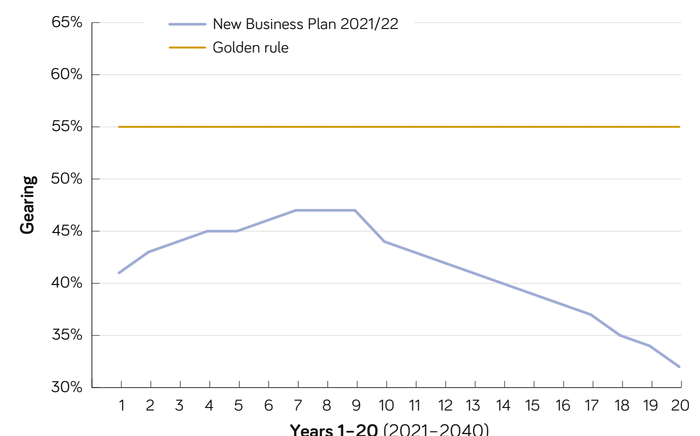
- ✔ Confirms compliance with the Regulator of Social Housing's (RSH) Governance and Financial Viability standard;
- ✔ Complements and provides resources to meet the 10-year ambitions in our Corporate Plan;
- ✔ Includes budgets for known building safety works and additional provisions for unforeseen works due to either building safety, changes to the Decent Homes Standard and our commitment to the decarbonisation agenda;
- ✔ Reflects the investment requirements of the stock condition surveys and complements the Asset Management Strategy;
- ✔ Reflects the costs of integration and efficiency savings as a result of the Transfer of Engagements of Equity Housing Group on 1 April 2020, in line with the Business Case approved by Board;
- ✔ Demonstrates continuing financial strength and capacity whilst achieving the latest development-led growth of 11,000 new homes over 10 years from the Equity merger; and
- ✔ Continues to adopt a suite of prudent yet realistic assumptions.

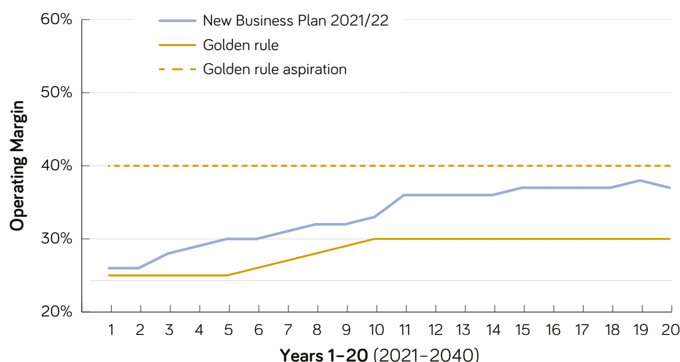
The contextual analysis that follows in section 2 shows that we are still operating in a period of unprecedented uncertainty and change. The business plan has been prepared taking into account this changing and uncertain environment, and those uncertainties have been tested to ensure that the Board are aware of any vulnerabilities within the plan.

The headline graphs are shown here with further analysis at section 4.









The sensitivity analysis performed on the new plan has demonstrated that the key sensitivities to the achievement of our golden rules are:

» property values falling for both shared ownership and outright sales live schemes which would have an immediate and significant impact on EBITDA MRI interest cover in year one;

» a further imposed rent freeze / cut which takes longer to impact golden rules i.e. by year 11;

» margin on future debt increasing by 2% could start to affect the plan from year three onwards with EBITDA MRI interest cover breaching golden rule in year six and covenant from year eight;

Also, any one-off shock with a financial impact in excess of £11.5m would see a breach of covenant in year one.

The numerous stress testing scenarios performed on the plan have outlined that the perfect storm would result if there was a Government imposed rent freeze which would result in a breach of EBITDA MRI interest cover covenant in year eight.

In prior business plans our unencumbered stock position, and therefore our ability to secure new funding was the most common constraint. The security position is significantly improved due to the bond sale. This plan shows that EBITDA MRI interest cover covenant breaches are more common in the stress tests and this is due to the significant budgets and provisions now included in the base case business plan for investment in our assets for building safety and retrofitting.

The base case assumptions are provided at Appendix A with details around the underlying economic assumptions as well as local assumptions around development units and tenure mix.

Purpose and context

GREAT PLACES HOUSING GROUP LIMITED – PARENT COMPANY

During 2020/21 and into the new financial year, work has been underway to simplify the Group's accounting structures and the intercompany trading mechanisms. All colleagues previously employed by Great Places Housing Group were TUPE'd into Great Places Housing Association on 1st March 2021. The main driver for this was to ensure that the pension liabilities were contained within Great Places Housing Association and effectively matched by the assets of the Group.

As a result of this simplification work, the only transactions flowing through Great Places Housing Group, the entity, is interest payable to funders, and the charge back of that interest to Great Places Housing Association.

The only assets held within the parent company are investments.

GREAT PLACES HOUSING ASSOCIATION

Around 90% of Group income and operating costs are generated in Great Places Housing Association and an even higher proportion of the operating surplus and the surplus after tax are also produced by GPHA.

The Group's asset and liabilities are even more weighted to GPHA, which owns almost 99% of the Group's total fixed assets and also has a similar proportion of the Group's debt and grant liabilities.

GPHA as an entity is therefore materially little different from the consolidated Group information reported.

PLUMLIFE HOMES LIMITED

All colleagues employed by Plumlife Homes Limited were successfully TUPE'd into Great Places Housing Association on 1st March 2021.

As part of the accounting simplification of inter-group trading, the majority of the property management activities previously undertaken by Plumlife Homes Limited will now be undertaken using the Plumlife brand, within the GPHA legal entity with the exception of any contracts in the name of Plumlife Homes Limited.

All debt relating to Plumlife Homes Limited has been repaid in the last financial year.

CUBE HOMES LIMTED

Cube Homes Limited (Cube) was established in August 2007 as a vehicle for the delivery of market sale activity for the Group and is a wholly owned subsidiary of Great Places Housing Association (GPHA). The purpose of Cube has been clearly set out as:

"To undertake profitable activity that will produce surpluses to help subsidise charitable activities within the Group"

The Cube business plan was approved by the Cube Homes Limited Board in March 2021 and is for the 30-year period from 2021/22. It is based on current live schemes, known pipeline schemes, together with forecasts and other assumptions. Whilst the plan reflects Cube's ambition, clearly the impact of the Coronavirus pandemic on the market and the supply chain is such that at present we cannot accurately predict future changes in this housing market. Thus far Cube has not been massively impacted, however new and existing challenges are still present. The operating environment continues to be extremely dynamic.

Cube's plan has been fully updated and demonstrates continuing financial strength and financial capacity to deliver at least £2m profit per annum, of which a minimum of £1m will be gifted to Great Places Housing Association.

The baseline Cube business plan delivers:

- Turnover forecasted to be £16.0m in 2021/22, rising to £19.9m in 2022/23
- Non development activity is primarily centred on market rent and the 143 market rented properties, of which Cube owns 45 and the other 98 are owned by GPHA.
- The market rent portfolio income is set to increase to £1.45m by the end of year 5 and £1.8m by year 10
- Surplus before gift aid and tax is above the £2m target in all years except year 2 where it is £1.9m
- Operating margin is at an average of 13.4% for the next 5 years
- 47 homes for sale to be built in 2021/22 and a total of 359 over the next 5 years
- Cube aims to gift aid £15.4m to GPHA over the next 10 years

TERRA NOVA DEVELOPMENTS LIMITED

Terra Nova is a Company Limited by shares which is a wholly owned subsidiary of GPHA. From 1st April 2021 the coterminous Board was expanded to include the activities of Terra Nova Developments Limited.

Terra Nova is a vehicle through which GPHA contracts to build affordable and social rent development schemes. The structure allows GPHA to recover much of the otherwise unrecoverable VAT on consultancy fees like architects, by consolidating multiple contracts into a single design and build contract with Terra Nova as a conduit.

During 2020/21 Terra Nova has also started to undertake in-house construction, including land-led development, with a number of schemes approved and the first schemes now on site. Future years' business plans will see more analysis for Terra Nova, but for now, the activity is relatively small and therefore no financial tables have been produced for this entity.

Any material taxable surplus in Terra Nova is gift aided back to GPHA, its parent. This structure has consistently produced VAT savings to the Group over many years, the benefit of which helps bring down scheme development costs.

REGULATION

The business plan, stress testing, mitigations and recovery plans set out in this document are key elements in showing that Great Places meets the requirements of the RSH Governance and Financial Viability standard. The development of the stress tests and mitigation strategies undertaken through discussion at the March Board away day demonstrates the Board's understanding and ownership of these vital processes, including the materiality of various influences, the impact of economic cycles as well as one-off shocks on the Group.

The business plan establishes strong financial performance against a suite of financial measures and VFM metrics, with golden rules in place for key funding covenants. The plan shows significant headroom against the golden rules which in turn provide material levels of comfort against the underlying covenants. The plan is not dependent on sales surpluses and the key EBITDA MRI interest cover covenant excludes surpluses on open market sales and asset sales but it does include first tranche sales surpluses.

The plan incorporates provisions for costs to fully meet all of the Group's likely remaining building safety liabilities by March 2023 and thereafter includes additional provisions, alongside fully funded stock condition survey requirements, to start the journey to net zero carbon across the entire portfolio.

The Group has strong liquidity following a highly successful £70m retained bond issue in January 2021. Towards the end of 2020 the Group's credit ratings with both Moody's (A3) and Fitch (A+) were reconfirmed, although Fitch have downgraded the UK sovereign rating as a result of the Coronavirus pandemic which resulted in all of their UK RP ratings, including Great Places, being given a negative outlook.

Great Places is currently in the midst of an In-Depth Assessment (IDA) being undertaken by the Regulator. The Group's previous IDA took place in Spring/Summer 2018 and gave a G1/V1 outcome. However an interim judgement published by RSH in April 2020 following the Equity merger combined Great Places' G1/V1 with Equity's G2/V2 and produced a compliant G1/V2 result. This IDA will be the first formal evaluation by RSH of the enlarged Group.

BUDGET 2021 ANNOUNCEMENTS

The main elements of Chancellor Rishi Sunak's March 2021 budget sought to avoid the post pandemic cliff edge by providing short term extensions to the furlough scheme, the £20 per week Universal Credit uplift, VAT cuts for hospitality and tourism and the stamp duty holiday. However the cost of the Covid support package and the impact on National debt was recognised by proposals to increase Corporation Tax from 19% to 25% from 2023 and also through the zero and higher rate personal allowances being frozen until April 2026.

The "Planning for the Future" White Paper was launched in August 2020. The main features of the White Paper include amending the standard method for calculating housing need, further changes to permitted development rights, a national levy to replace the current system of developer contributions (including section 106 arrangements) and the designation of all land as either "growth", "renewal" or "protected areas".

Government policy is also promoted through the £12bn Affordable Homes Programme (AHP). This includes a new approach to the Shared Ownership model with first tranches starting at 10%, staircasing in 1% shares, and a ten-year repairs and maintenance obligation on the landlord. The AHP requires 50% of new homes delivered to be home ownership products, whilst all rented homes will provide a "Right to Shared Ownership" to allow tenants to purchase a share of their home.

This business plan is predicated on Great Places being successful in retaining its Homes England Strategic Partner status. The bidding process formally opened in mid April 2021 and results are not expected until the Autumn. In the meantime, to help enhance the deliverability of a 2021-2026 Great Places Strategic Partnership, the Group continues to build its forward pipeline of new schemes, in advance of having grant funding in place. This is a risk that has been considered in depth and approved by the Board, as are all individual schemes in that position.

HOUSING MARKET

With a development programme that has a significant shared ownership sales element, together with Cube's profit-making outright sales activity and a not immaterial volume of "statutory" sales such as right to buy, right to acquire and staircasing, the housing market is an important consideration for the Group.

The housing market, particularly outside London and the South East, has remained remarkably resilient during the pandemic, at least in part strengthened by the stamp duty holiday. UK House price index data published in January 2021 by HM Land Registry showed that the average price of a property in England was £266,532, with an annual increase of 7.5% but a monthly reduction on 0.6%. Price growth for new-build homes was 9.1% and for existing homes was 6.8%.

The North West was the fastest growing region with annual growth of 12.0% in the year to January 2021, and with increases in excess of that average in areas such as Manchester and Oldham. The worst performing local authority in which Great Places operates was Lancaster with a still healthy average increase of 8.6%. Price growth in Sheffield was 11.0%. By contrast, over half of the 32 London Boroughs saw house prices rise by less than 5% and in three Boroughs prices actually fell.

Across England, semi-detached houses showed the biggest increase out of all property types, growing by 9.1% in the year to January 2021 to £255k. The lowest annual change was in flats and maisonettes which increased by 2.0% in the year to January 2021 to £228k.

UK Property Transaction Statistics published by HM Revenue & Customs report that on a non-seasonally adjusted basis, volume transactions increased by 8.7% in England in the year to November 2020.

It is always a challenge to predict the future for the housing market, but many forecasters do attempt to do just that. Data released by Savills in the first quarter of 2021 predicted UK house prices to rise by between 3% and 4% over each of the 5 years 2021-2026, giving a cumulative increase of 21%. Regional variations were very evident with London prices rising by only 12.6% and prices in the North West and Yorkshire and the Humber rising by over 28%.

Whilst these forecasts provide some comfort, Great Places is not complacent about sales risk. The development programme maintains the well established policy of spreading sales risk by operating multiple sales outlets across the Group's wide geography, primarily of family homes in suburban locations. The plan includes close to 300 shared ownership sales in 2021/22, with around 25% of those already reserved.

Strong house price inflation is not necessarily a measure of an effective housing market. The affordability of homes becomes increasingly challenging if house price increases continue to outstrip earnings growth, a challenge that applies to both purchasers and renters. The Great Places business plan does not incorporate house price inflation of the scale suggested by Savills and the overall plan is not dependent on surpluses delivered through sales.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE (ESG)

During 2020/21 an independent triennial governance review was completed, that confirmed that Great Places is fully compliant with its Code of Governance, which is an enhanced version of the 2015 NHF Code. The Group plans to adopt the new 2020 NHF Code of Governance during 2021/22. During the year the Group will commence the first stage of a two-year Board succession and recruitment process which will see five of the existing Board step down as they reach the end of their tenures.

Great Places has signed up to be an early adopter of the ESG Reporting standard and will produce its first ESG report for the year to 31st March 2021 alongside its Financial Statements. This will reinforce the Group's strong ESG credentials that are demonstrated by commitments including the achievement of EPC C by 2028 and being a carbon literate "Project Platinum" organisation.

ACCOUNTING AND TREASURY

There are no known major accounting changes expected to impact forthcoming financial years.

The March 2021 accounts will include the fair value gain on acquisition relating to the merger with Equity Housing Group. For the purpose of this business plan, the overall figure has been estimated at c£40m but will only be finalised as part of the March 2021 external audit process. There are individual fair value adjustments on the balance sheet specifically within housing properties and loans which will be amortised over the life of the assets or the life of the loan.

The Group continues to work with our funders towards a new basis for calculating interest rates. The current LIBOR (London Interbank Offer Rate) arrangement is to be replaced by SONIA (Sterling Overnight Index Average) as the benchmark for sterling variable rate loans and derivatives by the end of 2021. The RPI measure of inflation will be amended from 2030 to be aligned to CPIH (Consumer Price Index with Housing costs). This technical change will have wide-reaching implications, the main one for Great Places being rents for shared ownership properties.

3

Main changes to the Business plan since last year

The last plan was approved in September 2020, therefore the majority of the changes since then relate to the re-forecasting of development spend based on actual performance and revised forecasts as well as an extensive budget setting process for year one of the plan.

The biggest change which has impacted the base case business plan is the inclusion of significant additional provisions for investment works to our properties whether its building safety works due to changes in legislation or regulation or retrofitting our properties to achieve our Corporate ambitions.

By the end of the Corporate plan period (FY2028) this business plan sees Great Places own or manage around 27,000 social housing homes, have a turnover of close to £250m, surplus of around £33m and housing assets at cost of almost £2.8bn. All of these would exceed the Corporate Plan ambitions.

Our ambition to deliver 11,000 new homes in the 10 years post the Equity Transfer of Engagements is still achievable, but only with the continued support from Homes England.

4

Base case

The base case business plan provides assurance that we can deliver on our Corporate Plan ambitions within the Board's financial risk appetite. This plan sets out the long-term financial plan from 2021/22 and meets all covenants and the golden rules for the full 30 years.

The main changes to the business plan relate to the re-profiling of development expenditure, and any resultant sales based on more up to date forecasts, increases in major repairs budgets for known building safety works and additional provisions, reduced rental income due to lower CPI and reductions to the previously charged Equity property rents.

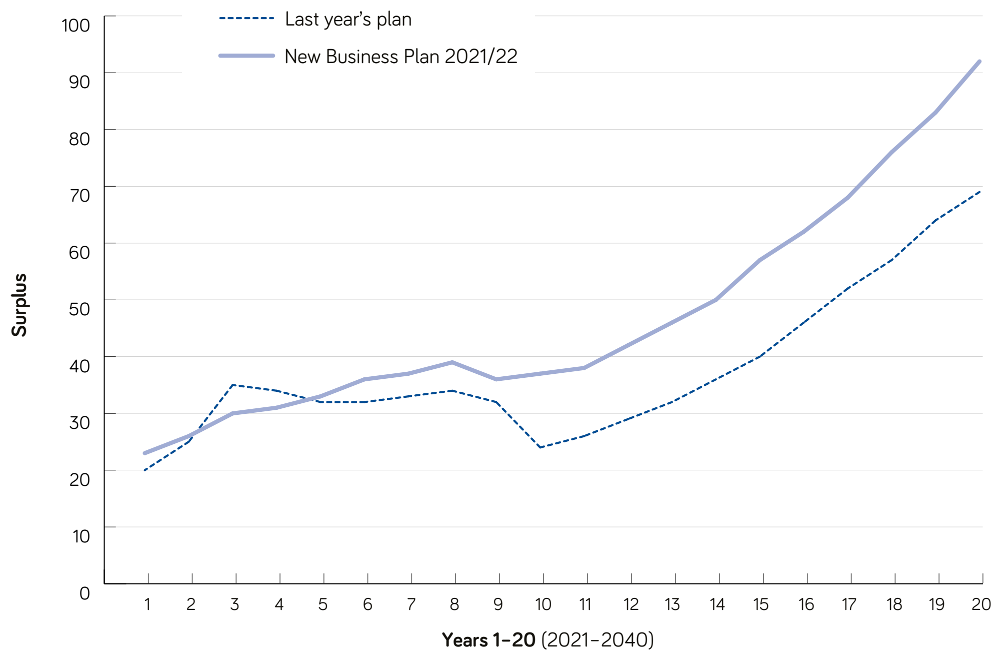
The base case also delivers close to 800 new homes in year one and a total of 5,700 by year five, of which 1,664 are committed via current Homes England programmes. The plan meets all golden rules and covenants for the length of the plan. Headroom against the golden rules and covenants are shown in the following table:

		Baseline Business Plan			
		To be better than	Worst Result	When	Headroom
Gearing (to be lower than)	Golden Rule	55.0%	47.2%	Year 8	£225.1m
	Covenant	65.0%			£514.3m
EBITDA MRI interest cover (to be more than)	Golden Rule	125.0%	133.0%	Year 11	£5,746.0k
	Covenant	110.0%			£16,531.1k
Operating margin (to be more than)	Golden Rule	25.0%	26.2%	Year 1	£2,026.1k

The following charts show the business plan outcomes compared with last year's plan and compared to the Group's golden rules.

GRAPH 1 – SURPLUS BEFORE TAX

Graph 1 shows the profile of surplus generated over the life of the plan. The deterioration in the surplus compared with the previous business plan is in the main due to the additional building safety, decent homes and decarbonisation budgets and provisions.



The annual surplus achieved in this plan grows steadily from £20m in 2021/22 to just over £127m by the end of the plan with a dip in year 9-10, which is mostly due to the cessation of Cube's market sales development as well as additional interest payable on additional borrowing required to fund the development programme. From year 10 we see a reduction in development expenditure and therefore a reduction in development overheads after the current development aspirations have been met.

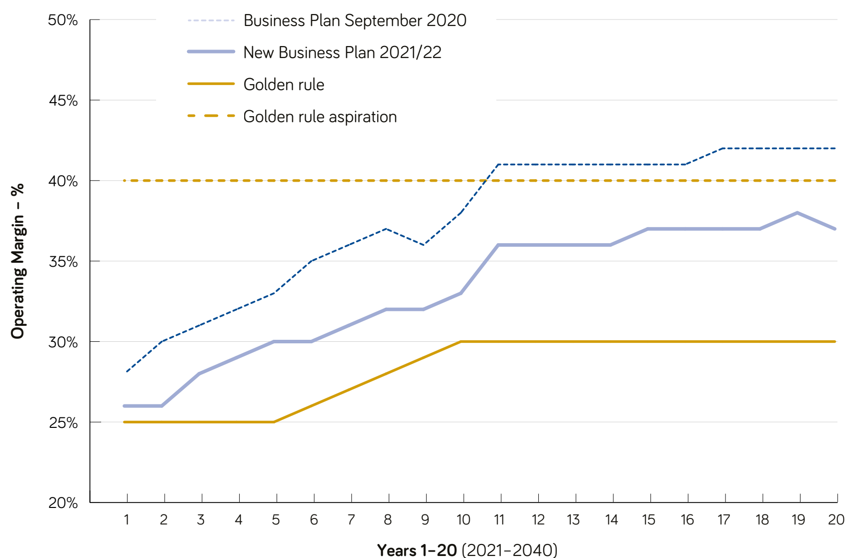
In the earlier years of the plan there is a significant revenue investment in systems and infrastructure to gain the benefits of the merger with Equity Housing Group as well as better manage the business continuity and disaster recovery risks. In an ever changing digital and tech world, we will start to see a shift to cloud based solutions, and solutions offered "as a service" which is revenue spend rather than the on premise capital spend we have seen in the past.

As noted previously, there is also an increase in costs due to building safety and decarbonisation throughout the plan and for the purposes of the surplus graph, around 80% of those costs are included due to the capitalisation of the other 20%.

GRAPH 2 – OPERATING MARGIN

Graph 2 shows the Group's operating margin (surplus before interest as a proportion of turnover) – effectively a measure of profitability. The importance of maintaining the operating margin is demonstrated by the adoption of this measure as one of the golden rules, with a minimum acceptable level of 25% for 5 years to then move steadily to 30% after integration, and an aspiration to move towards 40% in the longer term.

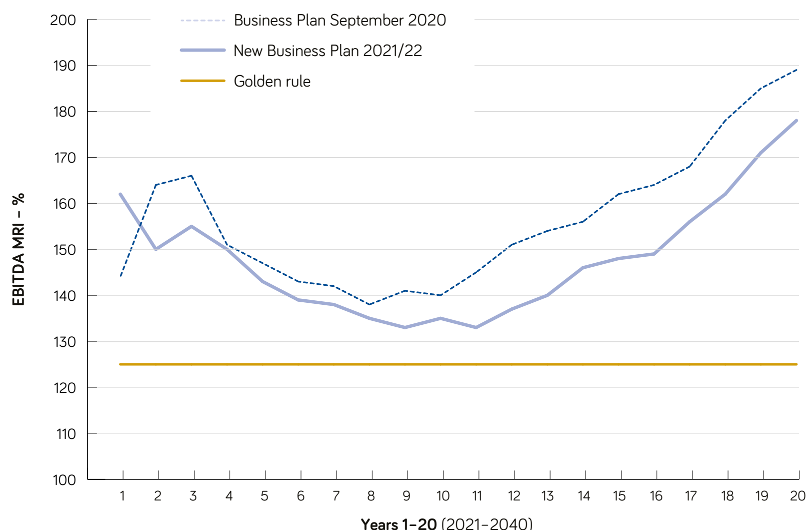
The factors affecting surplus also affect the operating margin. From year 10 there is a sharp increase in operating margin, depicting the end of the Cube business plan, where a higher proportion of "relatively" low margin (but of course very profitable) open market sales undertaken dilutes the Group's operating margin in the earlier years, with operating margin reaching 38% by the end of the plan.



GRAPH 3 – EARNINGS BEFORE INTEREST, TAX, DEPRECIATION AND AMORTISATION (MAJOR REPAIRS INCLUDED) INTEREST COVER

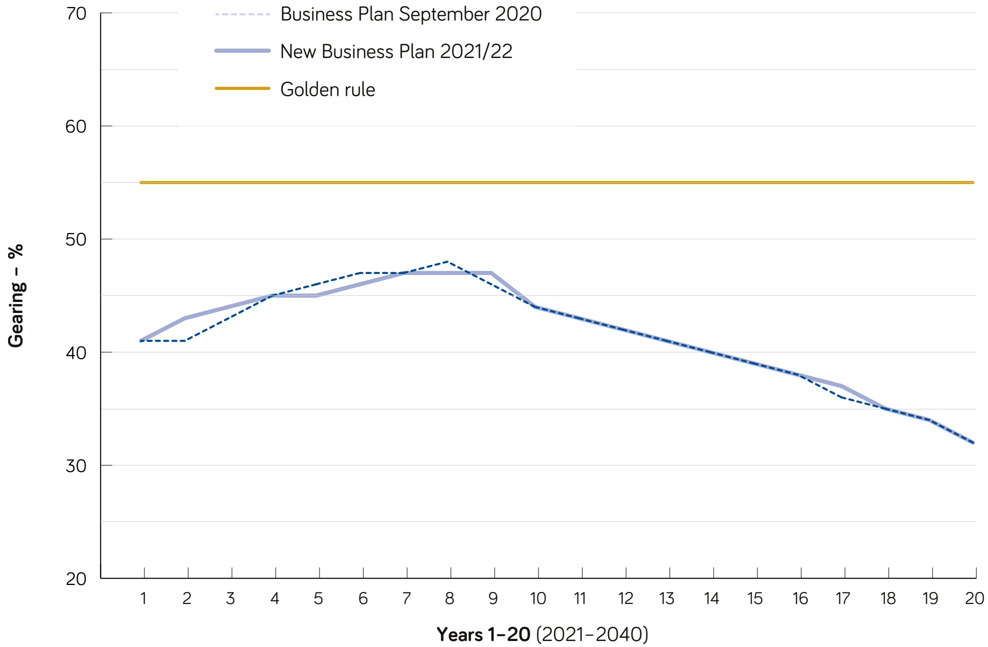
EBITDA MRI interest cover is the covenant that demonstrates our ability to service our debt. The tightest EBITDA MRI interest cover covenant is 110%, therefore the golden rule has been set at 125% providing an additional 15% headroom in interest payable, or operating costs, which equates to approximately an additional £10.8m headroom in the tightest year, being year 11.

The new plan shows a deterioration in this metric when compared to the previous plan again reflecting the items which affect surplus and operating margin. After year 10 the trend is similar to the previous plan with an ongoing steady increase driven by increasing surplus and operating margin.



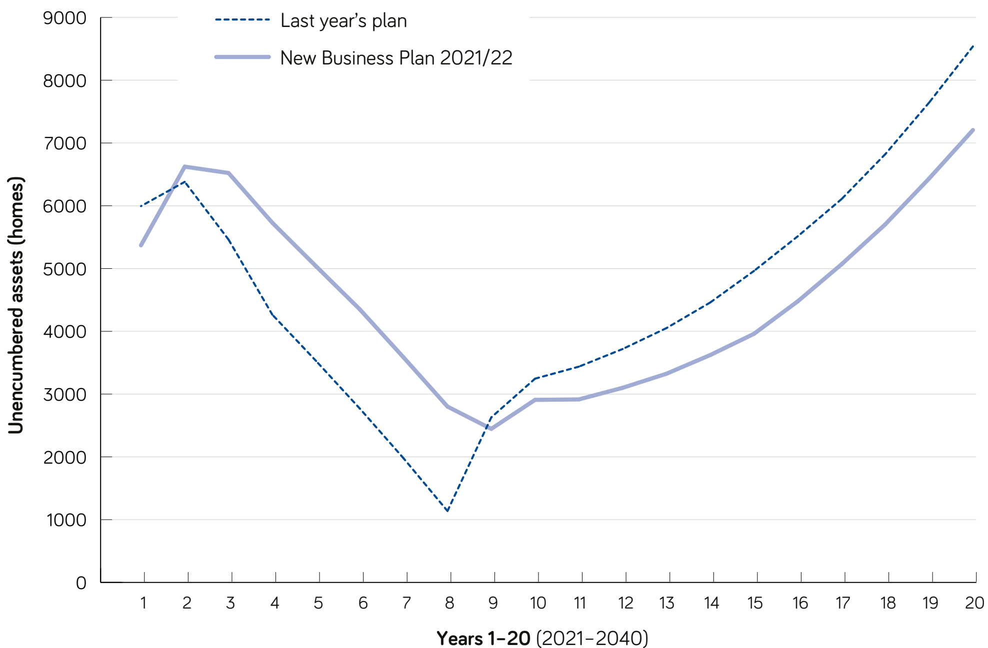
GRAPH 4 – GEARING

Graph 4 compares the Group's debt net of cash to the asset base (measured as housing properties at cost) and has a funding covenant maximum of 65%, and a golden rule set at 55%. The plan remains comfortably better (i.e. lower) than the 55% golden rule.



GRAPH 5 – UNENCUMBERED ASSETS

Graph 5 shows how the business plan impacts on the unencumbered assets of the Group. The Group currently has just over 4,500 unencumbered properties and this rises for two years as there is no requirement to charge properties over this period and as we release properties due to loan repayments. We then see it steadily fall through to year nine as we hit the peak of new development to meet our 11,000 homes ambition, with the associated new debt requirements from around May 2023. After year 10 development volumes reduce and the pool of unencumbered assets begins to increase.



FINANCIAL METRICS

In aggregate, the RSH Global Accounts state that the average headline social housing cost has increased from £4.12k per unit in 2019 to £4.25k per unit in 2020, an increase of 3%. The table below depicts the Regulator's VfM metrics based on the new business plan, with a comparison to previous years and comparing Great Places to the sector averages within the Global Accounts.

RSH VFM metrics	RSH Median 2019/20	Great Places 2019/20	Great Places draft results 2020/21	Great Places budget 2021/22
Operating Margin – overall	23.1%	28.6%	25.7%	26.2%
Operating Margin – Social Housing Lettings	25.7%	34.2%	28.1%	32.1%
EBITDA MRI Interest cover	170%	145.8%	148.6%	153.0%
New Supply: Units developed as % of units owned	1.5%	1.3%	1.3%	3.7%
Gearing	44.0%	46.8%	44.0%	43.5%
% Reinvestment	7.2%	5.1%	6.9%	11.3%
Return on capital employed (ROCE)	3.4%	3.3%	2.7%	2.9%
Headline social housing cost per unit	£3.8K	£3.3K	£3.4K	£3.3K

Note the definitions used in the VFM metrics are not the same as those used in the Group's funding covenants or golden rules.

The following table shows the VFM metrics for the next five years demonstrating the position improving across most of the measures.

RSH VFM metrics	2022	2023	2024	2025	2025
Operating Margin – overall	26.2%	26.5%	28.3%	29.2%	29.7%
Operating Margin – Social Housing Lettings	32.1%	31.2%	35.0%	35.9%	35.8%
EBITDA MRI Interest cover	153%	154%	161%	156%	149%
New Supply: Units developed as % of units owned	3.7%	5.1%	4.9%	4.3%	4.1%
Gearing	43.5%	45.6%	46.7%	47.9%	49.1%
% Reinvestment	11.3%	11.9%	15.1%	13.8%	13.1%
Return on capital employed (ROCE)	2.9%	3.0%	3.4%	3.3%	3.2%
Headline social housing cost per unit	£3.3k	£3.4k	£3.4k	£3.4k	£3.3k

The table below shows a summary of the total capital expenditure planned for 2021/22 along with the sources of funding for this spend.

Area of spend	Budget £'000
Development of social housing properties	162,734
Development of market sales properties	12,270
Capitalised major repairs	10,820
Office refurbishments	572
IT Capex	2,448
Total	**188,844**

Source of funds	Forecast £000s
Use of existing loan facilities and cash generated from operating activities	128,725
Grant	11,417
Market sales receipts	14,850
Staircasing and other sales receipts	12,722
1st tranche sales receipts	21,130
Total	**188,844**

The following table shows the facilities that are available to the Group (this is not a complete loan facility table, it just shows loans which are not fully drawn). Of the £138.6m which is undrawn, £121.0m is already secured and can readily be drawn. The revised Treasury Strategy which will outline the funding requirements of this business plan will be presented to Board in July 2021. There is sufficient cash and facilities to meet all if the committed development expenditure and the plan shows there is a funding requirement from May 2023.

	Facility £000s	Drawn £000s	Undrawn £000s	Secured and available £000s
Santander RCF	43,830	0	43,830	43,830
NatWest GPHG RCF	30,000	0	30,000	30,000
NatWest GPHA RCF	55,000	199	54,801	47,144
Warrington BC	18,736	8,736	10,000	0
Total	**147,566**	**8,935**	**138,631**	**120,974**

At 31st March 2021 the Group held £138m of cash.

5

Stress testing

We undertake a number of sensitivity analyses on the business plan, where we change one variable at a time to see the effect on our metrics. Stress testing takes sensitivity analysis further by including multiple factors which could arise in certain shock events. The following stress tests have been modelled through the business plan and prepared using the shock event described.

A regulatory downgrade to a non-compliant position was considered by the Board at the away day in March 2021. As we have effective controls and assurance in place across all the risk areas, and over the medium term of the business plan we should not be at significant risk of a Governance or Financial viability downgrade. If it happened, the two most obvious impacts would be the loss of available grant funding for future developments, and higher cost of funding. Both have been tested in the sensitivity analysis.

STRESS TEST #1 – BUILDING SAFETY AND DECARBONISATION

This stress test shows additional costs in relation to building safety, either as a result of intrusive Fire Risk Assessments or as a result of requirements in the new Decent Homes standard and additional costs of retrofitting our current portfolio over and above the budgets and provisions already in the base line business plan.

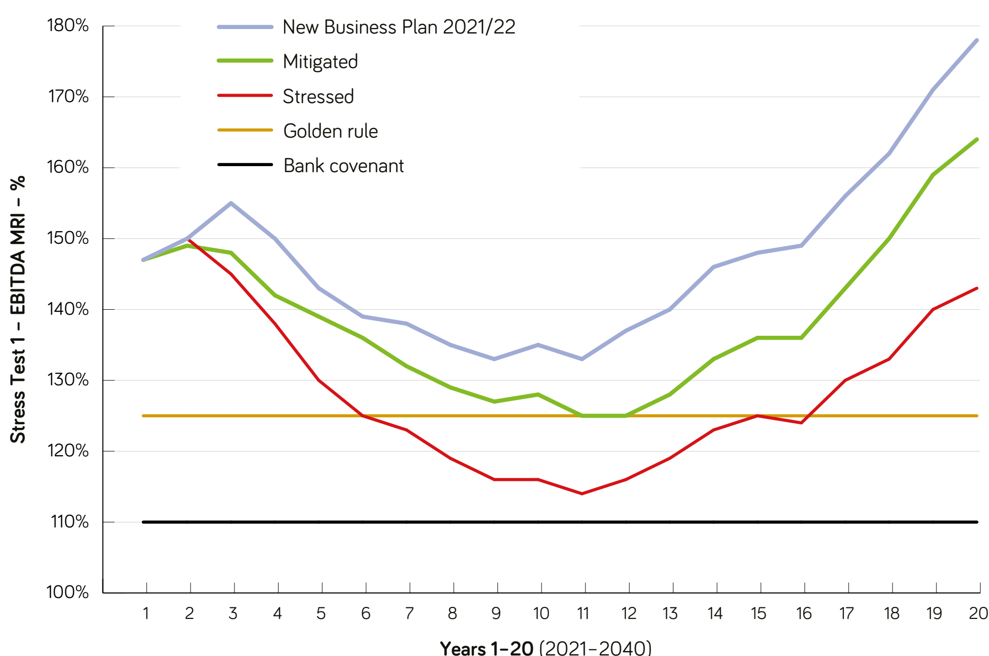
The Board are very clear that building safety is a priority and we would not defer urgent safety works, while recognising that risks may be managed and mitigated with temporary low-cost options. For new requirements in the Decent Homes standard the detail and timeframe of expectations will drive the prioritisation of work over time and whilst the regulation will be mandatory we would consider a phased approach. Retrofitting with the aim of net zero carbon is required in the medium to longer term but the costs would be significant. We can also show our new developments having additional costs, with no additional grant receipts. To model this shock event we have added an additional £2.5m provision each year from year three to 30, with a 20% capitalisation rate as well as increasing the costs of new developments by around £25k per unit.

The main impact is to EBITDA MRI, breaching the golden rule of 125% in years 7 to 16 because this stress test involves increased major repairs expenditure from year three, which is added back to EBITDA in the bank covenant calculation for interest cover. The lowest point is 113% in year 11. The result in this stress test never gets so low as to breach the tightest bank covenant.

The effect of the increased building costs for new developments impacts adversely on Security exhaustion, which runs out in year nine, and somewhat on Gearing which rises to 50.5%, also in year nine.

The mitigations with the most effect are to scale back future development, inviting Strategic Partnership delivery partners to deliver some units, and phasing other component replacement works. For example in this mitigation we reduced costs by £1m in years 5–11 and then increased costs by £1m in years 12–17, both subject to inflation. With mitigations in place the total number of homes delivered over the ten-year period is only reduced by around 1,000 homes.

The graph here shows the effect of this stress event with the red line and also shows the recovery with mitigations in place, the green line.



STRESS TEST #2 – LEGISLATION: RENT FREEZE, RIGHT TO SHARED OWNERSHIP, VOLUNTARY RIGHT TO BUY.

We know the current Government are keen on home ownership and, although we don't have all the information yet, Board were keen for Right to Shared Ownership and Voluntary Right to Buy to be included in a stress and for it to include a Government imposed four-year rent freeze. The three elements have been modelled as follows:

Right to Shared Ownership

- Some of the new grant funded affordable rented units built in years two to seven under the Homes England Affordable Homes Programme 2021-26 could potential be included in the Right to Shared Ownership. Not all customers will take up the scheme, so we have assumed that 20% of new build units convert from affordable rent to shared ownership the year after completion;
- As a result of the increase in administration burden from more frequent sales and staircasing we have increased costs by £75k per annum for salary and legal costs;
- The surplus from first tranche sales has not been added to the stress test, and neither has the lost rental income as they offset and are less material than the change to security levels.

Voluntary right to buy

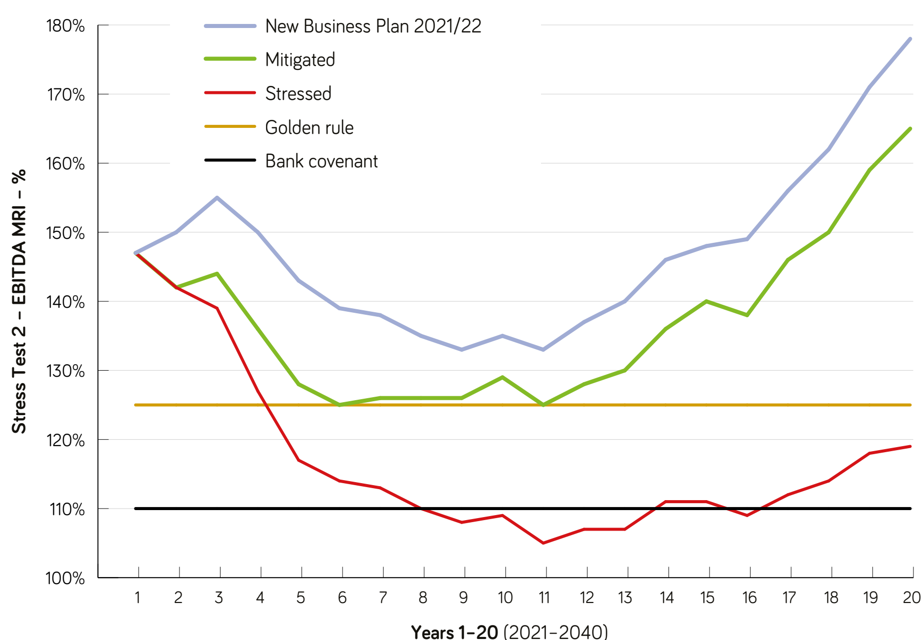
- We have assumed Voluntary Right To Buy of 50 general needs properties being sold each year from year three to year seven. Costs are kept in line with the baseline budget for Right to Acquire and other disposals, but we have only assumed a £5k surplus per sale.

Rent

- A general needs rent freeze in years two to five, restored to CPI only thereafter.
- Independence and Wellbeing (supported housing) rent inflation reduced to CPI only in years two to five.

The biggest impact in this stress test is the rent freeze. The lack of rents receivable, and the knock on effect of extra borrowings and higher interest costs means that EBITDA MRI breaches the golden rule from year three for the rest of the plan, and more significantly breaches the covenant from year nine. Unencumbered assets has very low levels from year nine onwards, never quite exhausting the security but very close throughout.

The mitigations needed a significant change that would materially deal with the rent cut: a reduction in all future development schemes by 20%, saving interest costs by reducing new borrowings. There was a range of other cost savings from the mitigations schedules that were used in this stress test, to illustrate the impacts of those.



After the mitigating actions have been implemented EBITDA MRI remains above the golden rule. Surplus and operating margin look broadly similar to the baseline business plan, albeit at a lower level throughout.

STRESS TEST #3 – PROPERTY MARKET COLLAPSE

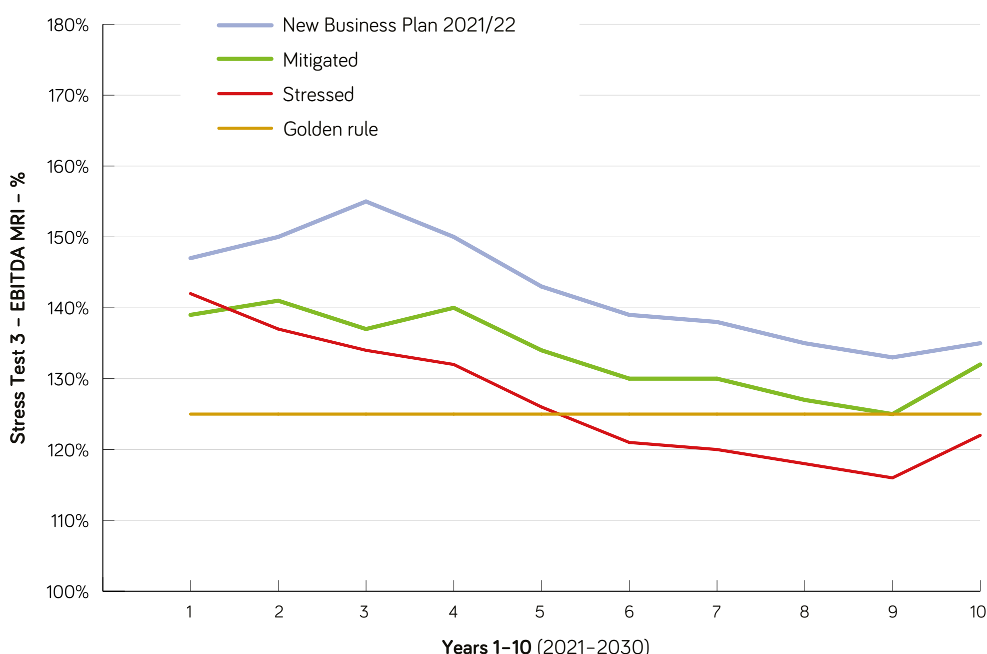
This shock event considers potential issues in the mortgage market either through a lack of affordability or availability or mortgages which may then delay sales. This multi variant scenario also includes a property market collapse, with a decrease in sales values too. The following potential outcomes have been modelled through the business plan:

- security values for unencumbered properties fall 5% in year two and freeze in year three, recognising that some properties are valued on the rental income streams, not the market value;
- 10% fall in property values in year two, followed by freeze in year three before reverting to the original CPI+1% assumption from year four; and
- sales periods for committed schemes lengthened, with the outright sales through Cube and the shared ownership first tranche sales being delayed over a three-year period.

In this shock event unencumbered assets are completely utilised by year nine, due to having to borrow money earlier and therefore charge properties for security.

The mitigation is about delaying the development programme by six months, whilst keeping the overall development programme the same. In the stress the property prices did fall and did not rapidly recover. By delaying the building for schemes not yet in contract, it helps to allay the impact of delayed sales for committed contracted schemes. An assumed one-off freeze (0% inflation) in year two in build and land costs as well as major repairs was also applied. If the housing market does decline, housebuilders will cut production which means less work for key trades, which will feed through to a reduction in build costs

EBITDA MRI and operating margin remain above golden rules, with some cost savings in years nine and 11 to allow this to happen. We modelled through additional management costs savings of £850k as a mix of reduced repairs and maintenance and other management costs in years nine and 11.



STRESS TEST #4 – UK ECONOMY: BREXIT, COVID, AUSTERITY MEASURES

This is a stress test to deal specifically with factors that might arise because of ongoing economic events like the pandemic and Brexit. This stress event is short term, recognising the particular challenges we face at the moment. Economic downturn and austerity measures could affect communities like the ones we operate in and may have an impact on commissioned Independence and Wellbeing services.

In this scenario we have modelled the following:

» Rent inflation at CPI only (rather than CPI+1%) as a potential austerity measure from central Government;

» CPI to increase to the Bank of England target of 2% over a five-year period, rather than two;

» Increased management costs due to austerity measures and Local Authority expenditure cuts (£1m in years one to three down to £0.5m in year five);

» The measures and cuts exacerbate issues in our communities, so we have assumed additional costs of £1.5m in years one to three, £0.75m in years four and five;

» Unemployment or reduced working hours and increased poverty, leading to sharp increases in bad debts to 3% immediately (instead of by year three) and voids (doubled in years one and two);

» Commissioned Independence and Wellbeing services needing additional subsidy; and

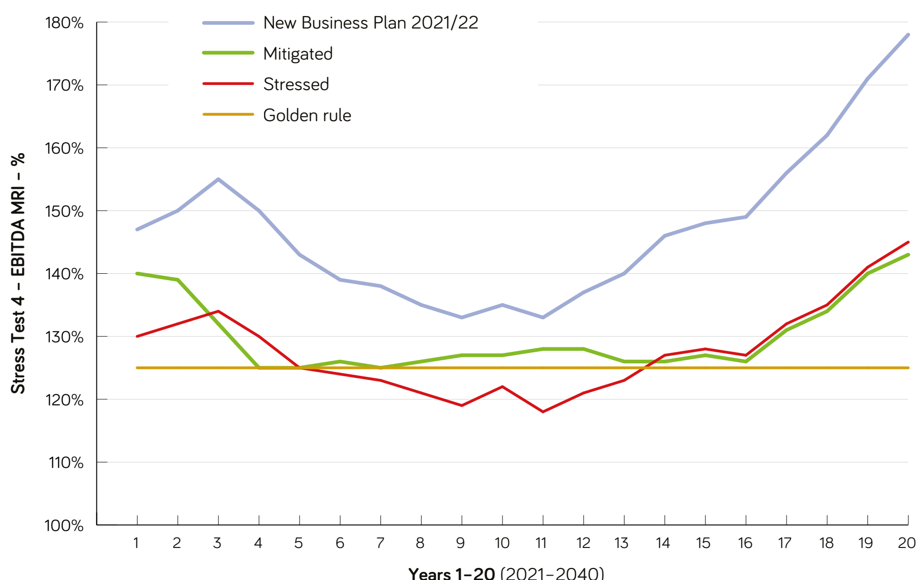
» Mortgage market may be less affordable: lack of mortgage availability or increased borrowing costs for our potential customers, impacting the surplus on shared ownership and market sales.

In this shock event EBITDA MRI breaches the golden rule in year five and gradually declines until the low point at year 11.

The mitigation plan for this stress event is mainly to delay non-essential major repairs that do not impair our regulatory or legal obligations. Other mitigations may be less suitable in this scenario, for example reducing some costs may exacerbate the issues in our communities felt most keenly in this stress test, like routine repairs and maintenance, discretionary capital investment in shared spaces, or ensuring that roles are filled quickly so we can deliver our service effectively. The delivery of new affordable homes is even more important in an economic downturn, so we have not reduced the development programmes in this stress test.

The quantum of the delays to non-essential major repairs are £2.1m in year one and £1.4m in year two with some catch up in future years but reducing overall by £0.8m. Again in years six to 13, deferrals of up to £3.8m in the tightest year to ensure EBITDA MRI is above the golden rule. It is worth noting again, that some of the amounts in the base case business plan are simply provisions and do not relate to stock condition survey data.

The Board may consider to waive the golden rules in these years, rather than reduce this expenditure in this economic environment. The bank covenants were not breached.



STRESS TEST #5 – BANK OF ENGLAND STRESS TEST

Each year, the Bank of England produces a stress test in order to test the resilience of the UK banking system and the individual institutions within it. The objective of the stress testing is to safeguard bank solvency. The stress tests consist of a set of macroeconomic assumptions for each scenario, which serve as a useful basis for Registered Providers to test their own business plans.

The 2021 Bank of England Stress Test largely follows a double dip scenario, where the macroeconomic shocks endured in 2020 (from the pandemic) are repeated and intensified. The scenario spans a five-year period and is characterised by:

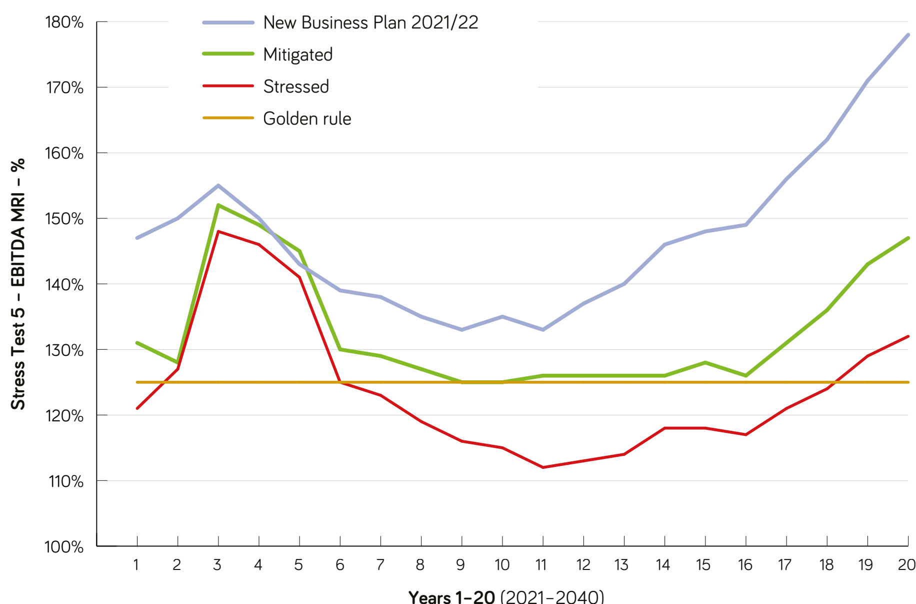
- Sharp unemployment, with certain sectors such as hospitality, construction and transport more affected than others;
- As a result of unemployment, sustained weakness in residential and commercial property prices;
- Due to significant uncertainty, consumers save, weakening demand;
- Persistently low interest rate environment (Bank Rate goes negative);
- Stress is felt globally, resulting in weaker equity prices and rise in bond spreads ; and
- Bank funding costs may as usual be passed through to borrowers.

Savills (our Treasury Advisors) have translated these assumptions into a recommended stress test scenario for Housing Associations.

The stress occurs straight away in year one with a breach of the golden rules (but not the bank covenant). EBITDA MRI drops to 120% and then rises rapidly to 150% by year three. Surplus drops to £9m in year one, recovering by year four. This is mainly driven by the property sales deflation/inflation in this stress test.

However the increased interest payable on new debt in years three to 20 means that EBITDA MRI breaches the golden rule from year seven to year 18 and surplus suffers, falling to £12m in year 10. Surplus recovers after year 10 because the development slows down and we borrow less.

The operating margin also breaches the golden rules in year one, being just 22.3%. It recovers after year five because it excludes interest. Long term security position looks good because of the property price recovery i.e. Unencumbered assets in the stress test is actually better than the baseline business plan.



The mitigations bring EBITDA MRI just above the golden rule. The results do not look as good as the baseline plan, but they do not breach rules, except for operating margin 24.2% in year one. This would breach a golden rule slightly, and Board would have to consider whether it would be prepared to accept this for one year to avoid reducing costs any more in this year. Further revenue cost reductions of £1.2m would have to be achieved to stay above 25% operating margin.

6

Mitigations

There are a number of mitigations which could be employed in any stress event if Great Places found itself in that perfect storm, the analysis shows that the recovery is achievable with covenants not being breached. Because of the permanent mitigations which are already in place, there would be time to enact recovery plans, and the Board are clear on which decisions management would take and which decisions would require further oversight and scrutiny.

Great Places has a number of permanent mitigations as follows:

- Minimum cash buffer of £15m;
- Minimum 75% fixed rate debt;
- Golden rules to provide headroom over funders' covenants;
- Underlying prudent assumptions;
- Asset and Liability register; and
- Early Warning Monitor.

There is also a framework of increased scrutiny around Great Places' contract management processes designed to mitigate potential counterparty risk. Governance and oversight has been strengthened around the contract management process.

The full mitigations schedule has been reviewed by management and Board and describes the mitigations that could be implemented by the Board or Executive in any given situation, along with details of potential risk and potential timeframes. There are two distint RAG ratings. The first is the ease with which the mitigation could be enacted. The second RAG is then a risk-based rating based on how this might affect Great Places' reputation, colleagues or strategic intent.

Should the need arise, and before considering any of these options, a full appraisal would be undertaken to understand the scale and timescales of potential cash or operating savings and any negative impacts or up front costs with particular reference to how the mitigation might affect the golden rules, cash, or reputation.

The mitigations are now split over three separate schedules:

1. Schedule 1 includes the levers that would be pulled if cash flow was the driver. There is inevitably an I&E impact but that isn't the main driver for these actions.
2. Schedule 2 shows the actions which will alleviate any risks to achieving golden rules / potential breach in covenants. That's the main driver although there will naturally be a benefit to cash as a result.
3. Schedule 3 describes opportunities that may present themselves in a stress scenario which Great Places could exploit.

Golden rules

7

The Group has adopted "Golden Rules" which set thresholds above or below which the Group will ensure it remains throughout its business plan. The Golden Rules are set at levels that are more difficult than the equivalent funding covenant, to ensure headroom is maintained at all times. These Golden Rules are set out in the table below:

Golden Rule	Description
Operating Margin	Operating margin before interest to be a minimum of 25% (and targeted to grow towards 40%)
EBITDA (MRI) Interest cover	EBITDA (MRI) Interest cover should not fall below 125% (covenants range from 105% to 110%)
Gearing	Gearing should not increase above 55% (covenant 65%)
Proportion of fixed/hedged debt	In line with approved Treasury Strategy (currently a minimum 75% fixed)

Great Places has a considerable shared ownership and outright sales programme, which makes up around a quarter of the Group's turnover and delivers an operating margin of around 10%–15%. This in turn dilutes the operating margin purely from that for social housing lettings which is at around 30%. The operating margin golden rule is at 25% for the first five years of the plan as we incur additional operating costs to fully integrate the activities of Equity Housing Group, with it then increasing gradually to 30% by year 10.

The tightest EBITDA MRI interest cover covenant is 110%. The golden rule has been set at 15% higher (ie. 125%) providing an additional £4.4m headroom in year one, over and above the current headroom of £11.0m, giving a total headroom close to £15.5m in interest payable or operating costs.

The base case business plan, and stress testing work does not suggest any amendment required to the golden rules as they stand.

The "Early Warning Monitor" is a tool to alert Board to any potential changes in the operating environment which could impact performance against the golden rules. The content and triggers will continue to be reviewed and updated on an annual basis – with proposals for 2021/22 being drawn up using this business plan stress tests and sensitivities as a guide and will continue to be reported to the Board via the Executive Director of Finance report.

Plan assumptions

8

We have assumed the following development pipeline, and the prior year numbers are shown to illustrate the ambition to develop 11,000 homes in the ten year period April 2020 to March 2030.

BUSINESS PLAN 2021/22		YEAR 1	YEAR 2	YEAR 3	YEAR 4	YEAR 5	YEAR 6	YEAR 7	YEAR 8	YEAR 9	
Year ending	March 2021	March 2022	March 2023	March 2024	March 2025	March 2026	March 2027	March 2028	March 2029	March 2030	TOTAL
Total social rent	44	38	206	172	145	145	145	145	121	121	1,282
Total affordable rent	159	463	533	460	442	442	442	442	640	649	4,672
Total shared ownership	129	291	403	500	442	442	442	442	415	415	3,921
Total supported housing	0	12	8	50	50	50	50	56	20	20	316
Total non-social housing	49	74	60	80	86	106	87	88	89	90	809
TOTAL DEVELOPMENT	**381**	**878**	**1,210**	**1,262**	**1,165**	**1,185**	**1,166**	**1,173**	**1,285**	**1,295**	**11,000**

This profile will inform the Homes England Strategic Partnership 2021-2026 bidding process and will in turn be updated later in the year should the outcome be materially different to that bid for.

Looking beyond the current programmes, we will look to utilise the additional capacity created by coming together with Equity to deliver our pledge to build 11,000 homes in the 10 years following the merger. After 2030, development is assumed to be an ongoing programme of 500 homes per year of around 200 shared ownership properties and 300 rented properties.

The following non-development assumptions have been made in the underlying business plan.

Assumption	Budget Yr1 2021/22	Year 2 2022/23	Year 3 2023/24	Year 4 2024/25	Year 5 2025/26	Years 6–30 2026/27+
3 month LIBOR	Rising to 2.50%	Rising to 3.00%	Rising to 3.50%	Rising to 3.75%	Rising to 4.00%	Rising to 4.35%
All in rate, variable rate debt	Rising to 3.90%	Rising to 4.40%	Rising to 4.90%	Rising to 5.15%	Rising to 5.40%	Rising to 5.75%
30 year gilt rate	2.00%	2.40%	2.80%	2.95%	3.35%	Rising to 3.65%
Future fixed rate debt	3.60%	4.00%	4.40%	4.55%	4.95%	Rising to 5.25%
CPI	1.70%	2.00%	2.00%	2.00%	2.00%	2.00%
Earnings inflation	CPI+1.50%	CPI+1.50%	CPI+1.50%	CPI+1.50%	CPI+1.50%	CPI+1.50%
General needs rents	CPI+1.00%	CPI+1.00%	CPI+1.00%	CPI+1.00%	CPI+1.00%	CPI
Universal Credit customers	6,291	8,716	100% potential UC claimants	100% potential UC claimants	100% potential UC claimants	100% potential UC claimants
Bad debts	Rising to 1.50%	Rising to 2.00%	Rising to 2.50%	Rising to 3.00%	3.00%	3.00%
Repairs inflation	CPI+1.30%	CPI+1.00%	CPI+1.00%	CPI+1.00%	CPI+0.50%	CPI+0.50%
Major repairs inflation	CPI+1.80%	CPI+1.50%	CPI+1.00%	CPI+1.00%	CPI+0.50%	CPI+0.50%
Construction price inflation	CPI+3.30%	CPI+3.00%	CPI+3.00%	CPI+2.50%	CPI+1.00%	CPI+1.00%
Land price inflation	CPI+2.00%	CPI+2.00%	CPI+2.00%	CPI+2.00%	CPI+1.50%	CPI+1.50%
Property price inflation	CPI+1.00%	CPI+1.00%	CPI+1.00%	CPI+1.00%	CPI+1.00%	CPI+1.00%
Building safety, retrofit, zero carbon & Decent Homes II etc.	£3.03m	£4.50m	£2.25m	£2.25m	£2.25m	£2.25m