

Clarion Housing Group **Value for Money** **Statement 2017**



CLARION
HOUSING GROUP

Value for Money Highlights

Clarion Housing Group is a business for social purpose. First and foremost we are a social landlord and our charitable aims are to house people who cannot meet their housing needs in the market. We build new affordable homes and we invest in maintaining our estate. Being efficient and effective is critically important. We do not distribute profits, so every penny we earn is reinvested in the business to deliver our charitable aims.

This year we completed the merger of Circle Housing and Affinity Sutton creating the largest social housing group in England. We firmly believe that the merger will give us the capacity to deliver significantly more than either party could have hoped to achieve on our own. Our ambitions are to create a cost effective, efficient, provider of services and developer of new homes.

This year in which we completed our merger was the beginning of our journey. This report highlights our plans for the future and the historic performance of the two predecessor organisations:

50,000

We expect to build 50,000 in a decade

2/3

Two thirds of our new homes will be below market for those in housing need

We expect to sell homes to other social landlords to release capacity which we will use to fund new homes. These homes will remain designated social housing and the sales should utilise previously under-utilised capacity.

£87m

We expect to complete the integration of Circle and Affinity Sutton releasing savings by year three of £87m compared to our pre merger costs, and bringing Clarion operating cost per unit down below those of Affinity Sutton. This represents a real terms reduction of 11% over 3 years.

£26m

We have set a budget for 2017/18 which will see operating costs reduce by £30m this year. In addition £26m of anticipated costs in 2017/18 are expected to be non recurring.

£10m

We intend to invest £10m per annum in community investment programmes to benefit our residents and to attract up to £5m of external funding each year

4,000

We expect to help 4,000 people each year into employment, and 1,500 youngsters to sustain their education and training

£100m

We expect to invest at least £100m each year in our homes, keeping them fit for habitation, warm and in a decent condition

£1bn

We have committed to significant investment in the regeneration of our existing homes, £1bn in Merton to deliver 2,800 new homes, as well as investment in Ealing and Westminster

We expect to have completed the simplification of the group and to continue to grow through building new homes and merging with others

We expect to roll out this financial year our new ERP systems with further investment in new and streamlined processes and ways of working, reducing costs and redirecting resources to create added value

Our Financial Golden Rules create a solid risk framework to balance essential financial strength with maximum investment in new and existing homes

Introduction

Both Affinity Sutton and Circle before merger had embarked on transformational change programmes. The driving force behind these programmes was to enable our customer offer to be as good as some of the leading customer service businesses in the country. We know from our customer insights that our customers increasingly want to access services digitally. Our current systems do not support that ambition. We also know that investing in new ways of working and new systems will deliver longer lasting efficiencies.

Given our commitment to providing a blend of excellent service and value for money we are investing in a major programme of business change that will transform the way we do business and further reduce our operating costs.

This Value for Money Report sets out Clarion's ongoing commitment to achieve value for money for our residents, stakeholders and investors. The report highlights a number of measures we have taken to drive further efficiencies, despite ongoing uncertainties in our operating environment, in addition to setting out our ambitious plans to transform the way we go about our business and the significant associated savings that this new approach will bring.

Our Financial Strength



Our approach to securing value for money and greater efficiency in our business is to expect and plan for savings to arise from growth, this will be savings from synergies we achieve post merger, and growth in homes we manage outpacing growth in our underlying operating costs.

This year the Group made a surplus of £173m on a turnover of £796m generating an Operating Margin of 36.4% which demonstrates a strong financial performance in a year of considerable change for the business. 90% of our turnover is derived from our core business of rents and service charges which delivered Social Housing Interest Cover of 150%, demonstrating strong underlying performance and showing that we place no reliance on asset sales or build for sale - just 10% is derived from development sales. As a business we have been keen to limit our diversification to what is required to support

our core social mission given dwindling government support for rented housing. Our plans for the next decade will see us develop a greater proportion of homes for sale, double our current programme, but we are committed only to doing what we need to be able to deliver our social housing ambitions.

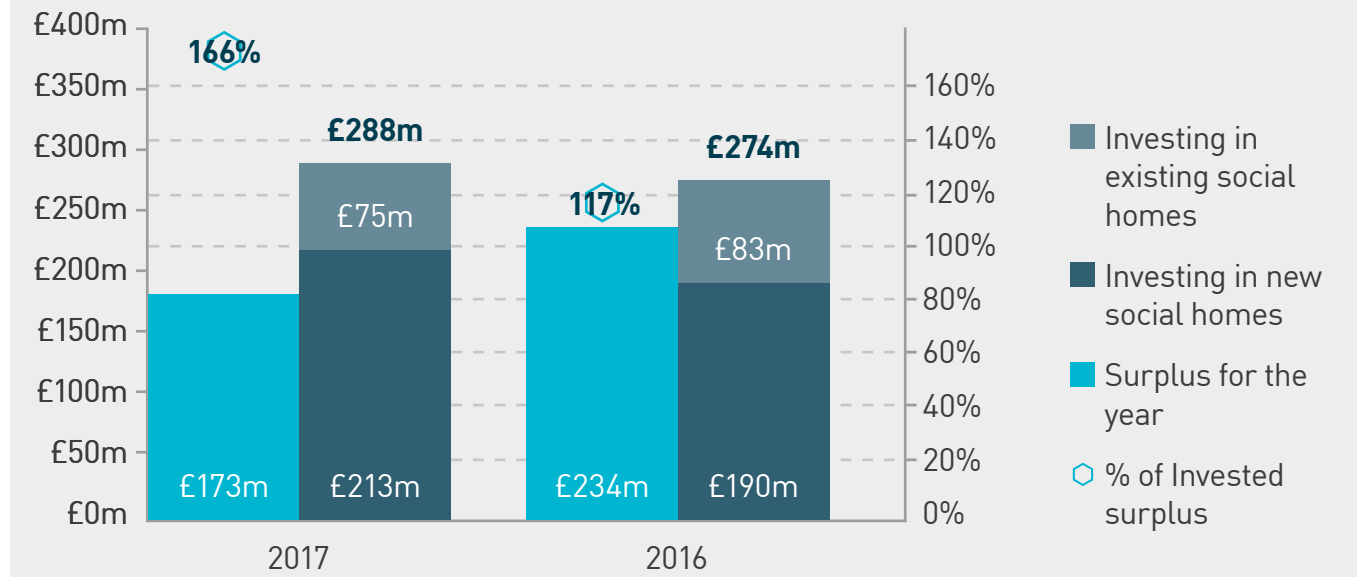
At 36.4% the operating margin of the group at year end remains strong despite some very real cost pressures in year principally arising from additional repairs and maintenance spend in Circle to rectify service failings in London.

EBITDA MRI which measures the headroom the business has from which to meet its long term interest costs is 200% at year end. Again this demonstrates the robustness of the financial position. Our 10 year forecast anticipates that EBITDA MRI will remain at or above 190%.

This year the Group invested £75m, which represents a long-term investment in our existing housing stock with an additional £292m invested in new homes for a range of tenures. We completed 1,340 new homes during the year and these homes were delivered with limited grant funding. For every £1 generated from operations we spent £0.73 on new homes, this is money generated from our own resources and demonstrates our commitment to investing in new homes in line with our charitable mission to provide homes for those excluded from the market. Running the business as efficiently as we can enables us to maximise this investment. During the year we started construction on 1,863 new homes, and at the year end we had 8,000 new homes in the development pipeline.

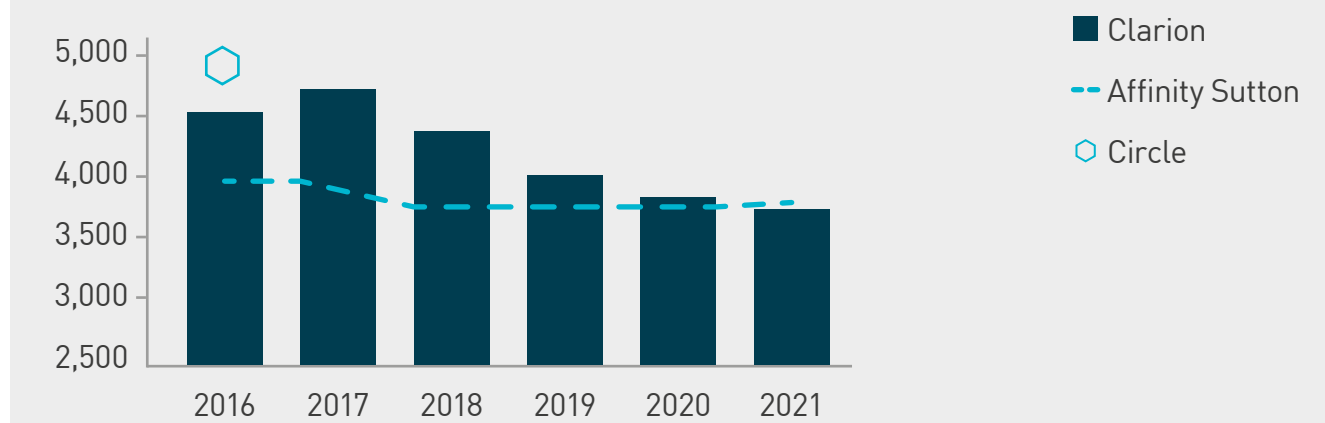
Our investment in new and existing social homes at £288 million, was 1.7 times larger than our annual surplus.

Our surplus investment in new and existing social homes



Our year on year focus continues to be to keep operating costs under control and to forecast no growth in underlying costs. The former Circle Group had operating costs of £ 4,935 per home, Affinity Sutton had costs of £3,970. At the year end the group had operating costs of £4,623 per home. Our clear ambition is to achieve costs which are lower than the operating costs of the former Affinity Sutton, which we expect to deliver within 3 years. We have made a start in agreeing the budget for 2017/18 with running costs which are £30m less than the costs in 2016/17.

Operating cost per unit



Each year we maintain a savings register and we validate all entries at the year end. This year specific efficiency initiatives across the group resulted in savings of more than £4m. Additionally we have delivered efficiencies of 8m which directly benefit our residents such as securing additional housing and other state funded benefits through work with our welfare benefit and income teams.

Delivering Social Value in our Communities

We run our business on commercial lines, with a keen eye on both efficiency and delivering value for money, and clear distinction between commercial and charitable activity. It is because of this that we are able to channel so much of the money we make into delivering social benefits for the communities in which we operate.

The work we have produced with HACT to develop a set of financial values which can be attributed to particular interventions is increasingly being adopted by other landlords in the sector. Being able to quantify the impact of our investment on people's wellbeing has proved invaluable not only in helping us to understand the return on our investment but also as we refine and develop our community investment programmes.

This year we have achieved a social benefit of £85m, this compares well with the previous year, not least as we had a reduced budget for community investment, and indicates improved performance in this.

Clarion's investment has a significant direct impact

on improving the lives of our residents and their communities. Post merger the Board has agreed to prioritise a significant increase in our spending on communities from just under £7m of our own resources to £10m. This will enable the group to offer a comprehensive service for all our residents wherever they live.

An important element of our community investment programme is our employment service. We believe that finding our residents work is the best route we can offer to financial independence and reduced dependency on welfare. Over the last year we have also been the lead agent for a group of housing associations who have rolled out employment services across London with funding from the Greater London

Authority and the European Social Fund. This year the service helped a record 1,745 people to find work. In addition to this, we also achieved another record by providing 122 apprenticeships, helping those young people to learn vital work skills.

Our community foundation, Clarion Futures has prioritised future investment in young people who are residents and the children of residents. Over the next few years we expect to be helping 15,000 young people annually to fulfil their potential through apprenticeships, training support and bursaries.

The Group continues to prioritise financial inclusion work and debt advice services which are more in demand than ever. Helping our residents to access affordable loans saved an estimated £16m in reduced payments and debt write-offs.

We have also continued to invest in Welfare Advice Services for our residents helping them to claim benefits which they are entitled to. This work alone has benefitted our residents by securing an extra £8.3m in income they would otherwise have foregone.



Our Assets

The Group has in excess of 125,000 properties across England. Some of these homes date back to the turn of the last century while others, for example those from local authority stock transfers were built in the 1950s, 60s and 70s.

It is incumbent on all housing associations to make the best use of their assets and we continue to improve on our approach. We have two main tools by which we inform our future investment and disposal decisions:

Estate Quality Index (eQual) is a qualitative scoring system for our estates based on a range of management and customer indicators, helping us understand how much effort an estate takes to manage and the desirability of the estate to current and prospective tenants. eQual is made up of tenant turnover, current tenant average stay, re-let times, contact volumes, account balances, void loss and repairs volumes. It is a robust and accessible tool which can be used to compare estates and can then be used to measure impact gained due to any interventions we make.

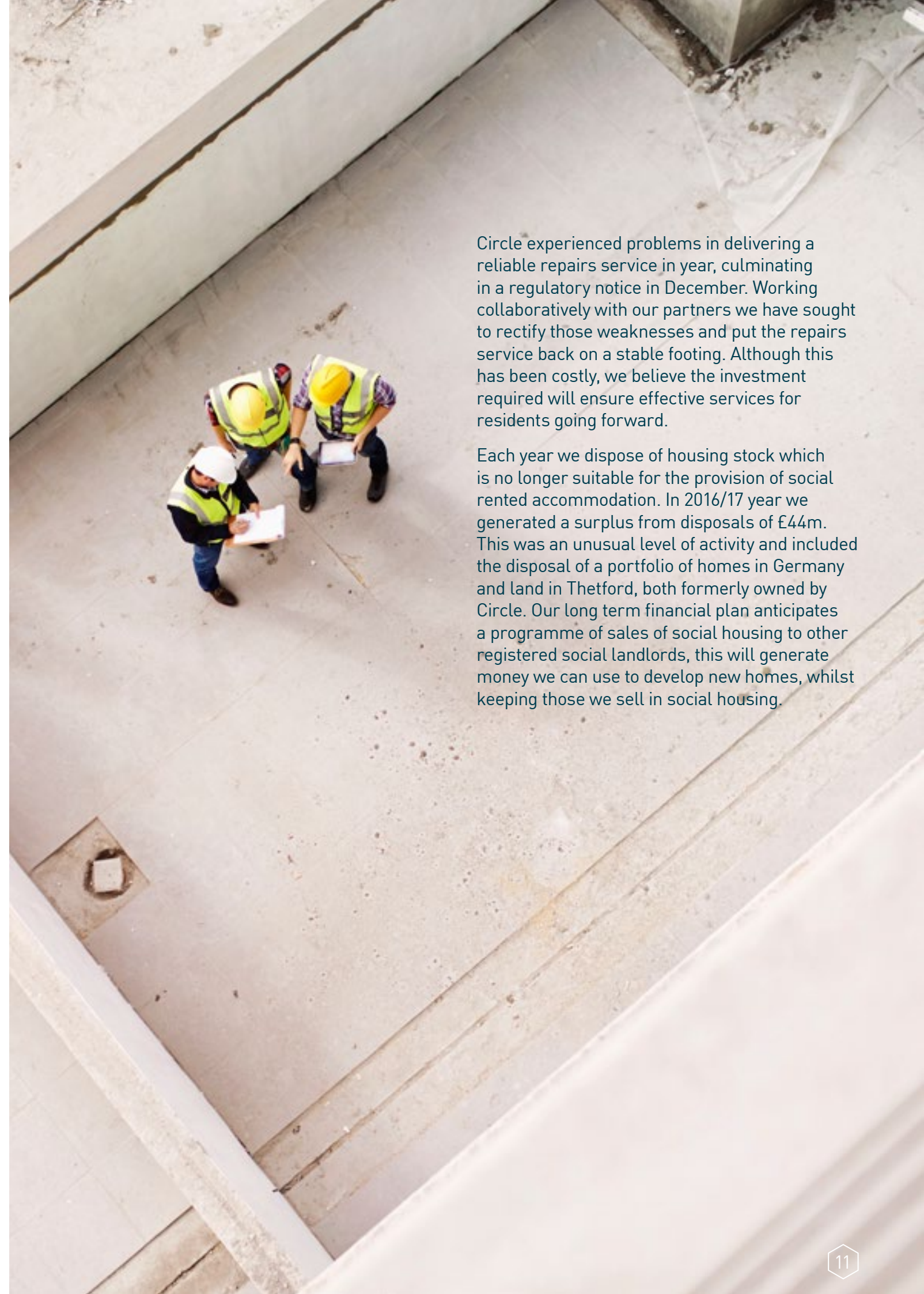
Estate Financial Model (eFin) is a discounted cashflow model that provides net present values, yields and vacant possession values for our properties, helping us understand how much our properties will make (or cost) us over the coming 30 years in today's money. Our reinvestment team use the eFin model to identify poorly performing estates based on their financial performance and carry out an options appraisal looking at the fabric of the buildings and wider environmental works involving a number of different departments in the organisation.

It is critically important that we manage our assets carefully in order that we derive the most value from them. Our total maintenance spend in 2016/17 was £ 279m, which reflects day to day

maintenance spend, investment in replacement components such as kitchens, bathroom, boilers and windows as well as energy efficiency, environmental and estate improvement works.

We have placed particular emphasis on helping our residents to make energy efficient choices to heat their homes. Working with residents to enable them to access the best tariffs, installing energy efficient measures in their homes and influencing behaviours has saved our residents in excess of £500,000 this year.

Last year the Group carried out 306,090 responsive repairs. At the year end Clarion was delivering 67% of all its repairs service in house through CBS, AS Repairs or Circle Housing Property Services. The remaining services were provided through contracts awarded to long term partner contractors. Post merger there is a significant amount of work to do to integrate both legacy services and to ensure the arrangements provide a good service for residents. We have taken several initiatives this year to improve the efficiency of our in house service including reducing the use of sub contractors, absorbing the impact of inflation on running costs and improving our void and empty property turnaround times, which together have saved the business over £800,000. These initiatives will be rolled out to the whole business this coming year.



Circle experienced problems in delivering a reliable repairs service in year, culminating in a regulatory notice in December. Working collaboratively with our partners we have sought to rectify those weaknesses and put the repairs service back on a stable footing. Although this has been costly, we believe the investment required will ensure effective services for residents going forward.

Each year we dispose of housing stock which is no longer suitable for the provision of social rented accommodation. In 2016/17 year we generated a surplus from disposals of £44m. This was an unusual level of activity and included the disposal of a portfolio of homes in Germany and land in Thetford, both formerly owned by Circle. Our long term financial plan anticipates a programme of sales of social housing to other registered social landlords, this will generate money we can use to develop new homes, whilst keeping those we sell in social housing.

New Homes

Clarion aims to be a developer of homes at a significant scale. Over the last year we have built 1,340 new homes across a range of tenures. Central to our development programme is ensuring we are able to focus on those who are failed by the market. Those homes were developed with just 9% of public subsidy, an average of £17.3k per home. Supporting a programme of this scale has required us to undertake commercial activities to generate returns to fill the gap left by shrinking public funds.

This year's financial surplus of £173m should be seen in the context of the £196m long-term investment we made in social housing over the last twelve months. Net of grant, we invested £179m into the construction of new social housing properties. Almost twice our annual surplus was applied to our core social housing activity through a programme of planned improvements, as well as the development of new social housing.

Transparency and Scrutiny

Our Group is committed to transparency. We publish detailed information about our spending, both on our website and in our financial statements. This year we have taken the opportunity to include in our value for money statement some of the metrics developed by the sector led Efficiency Working Group which we think helps illustrate the outcomes we achieve.

Our website contains details of payments to our top suppliers, action taken to combat tenancy fraud, delivery performance on our affordable homes programme, our current regulatory rating, our code of conduct and the results of resident scrutiny. Our Annual Accounts show details of the pay and reward offered to our staff and board, as well as key statistics and performance information.

Our residents remain at the heart of everything we do. Our Regional Scrutiny Boards (RSBs) and Service Improvement Panels, for example, are engaged in examining our performance in core areas of the business and making service improvement recommendations to the Board. This has included recommendations on door entry systems, communal lighting, untidy gardens, measuring success, and the roles of estate based staff.

Procurement

The Group maintains a savings register which is independently verified and lists all savings achieved through procurement. We strive to consistently realise savings in procurement on a year on year basis delivering value through both tender processes and contract management.

Procurement aims to ensure value for money is achieved at the awarding of contracts and extends to strategic delivery. We expect to deliver additional value from the tender process as well as ongoing contract management.

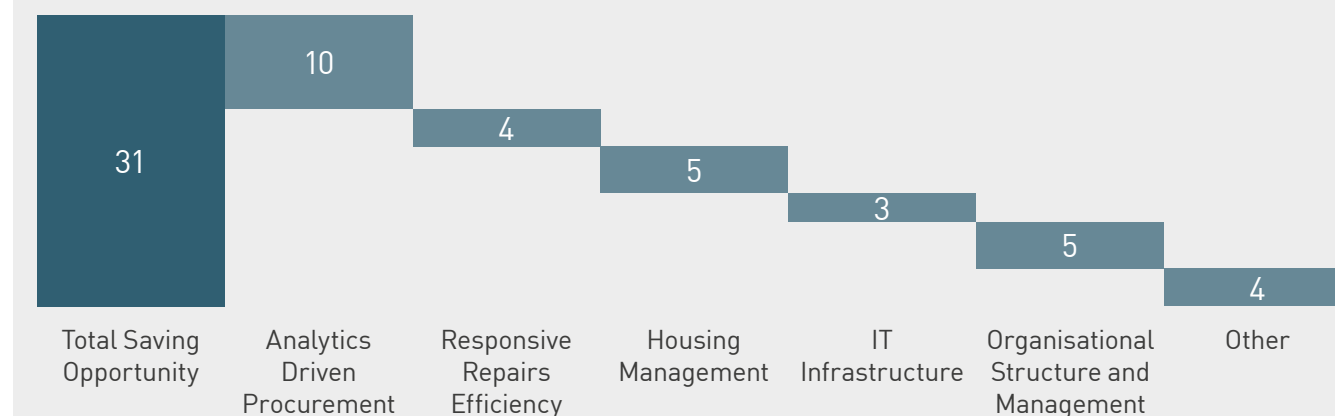
Since the year end we have commenced a programme of retendering services as part of or integration of the two merged businesses – this has realised projected savings for future years of £4 million from lifts and domestic gas service contracts.

Transforming the way we do Business

The Group recognises that simply driving cost savings will ultimately result in diminishing returns and also runs the risk of reducing levels of service. In order to mitigate this we are nearing the “go-live” of our major programme of transformational activity that goes beyond traditional continuous change processes and which will deliver ongoing benefits to residents and a significant return on investment.

There are significant savings opportunities for Clarion in the areas of Business Intelligence and Analytics, Responsive Repairs, Available Homes Management, Customer Visits and the Technology Estate.

Current potential cash saving opportunities (£m)



This group-wide change programme, ‘FF2’ will result in a transformation of service provision, working practices and customer experience. To underpin this change, we are working in partnership with Hitachi to deliver a Microsoft Dynamics Enterprise Resource Planning (ERP) IT platform.

The programme is now well advanced. We are have developed all-new business processes as a result of this exercise and are nearing the end of the critical “build” phase of the programme, before testing and go-live later in this financial year. These changes will ensure that the business is equipped for future growth in line with the Group’s ambitious growth strategy as well as providing an outstanding level of service to our customers, staff and business partners.

The Future Foundations Programme will deliver in three key areas:

- Customer – improving our service offer and the way we communicate with our residents
- Ways of Working - improving the way we deliver services and do business; and
- Technology - implementing the new ERP system

This programme is ambitious and timely, and it is unique in the sector. It will provide an integrated solution which is scalable for the business and which we can use as a platform to grow.



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