Homes & Communities Agency

The Social Housing Regulator

HCA Regulatory Judgement on
Southway Housing Trust – L4507

February 2014

The provider

Southway Housing Trust (Southway) was registered in November 2007 to receive a partial transfer of housing stock from Manchester City Council. Southway currently owns around 5,900 homes located in the south of Manchester.

Southway's primary focus is the management, maintenance and development of affordable rented housing. It employs around 187 full time equivalent employees and its turnover was £25.5m in 2012/13.

Southway has entered into a Short Form Agreement (SFA) with the HCA to deliver 28 new homes for affordable rent from 2011-17. Under the SFA, the delivery of the new units will be supported by charging affordable rents on a proportion of Southway's existing stock, rather than by the receipt of grant from the HCA.

Reason for publication: Viability upgrade.

Regulatory Ratings*

- **Properly Governed: G1**

The provider meets the requirements on governance set out in the Governance and Financial Viability Standard.

- **Viable: V1**

The provider meets the requirements on viability set out in the Governance and Financial Viability Standard and has the capacity to mitigate its exposures effectively.

*The regulator's assessment on compliance with the Governance & Financial Viability Standard is expressed in gradings from G1 to G4 for governance and V1 to V4 for viability. For both viability and governance the first two grades indicate compliance with the standard. A G3 or V3 assessment indicates a level of concern with the organisation's performance that is likely to be reflected in intensive regulatory engagement. A G4 or V4 judgement indicates a failure of governance or viability to the extent that the regulator is using its statutory powers.

Regulatory Judgement

The regulator's assessment of Southway's viability has been upgraded to reflect an improvement in its financial position since the previous publication in April 2013. In reaching this judgement the regulator has reviewed Southway's latest financial forecasts in conjunction with its strategic plan and held discussions with the executive.

The regulator's previous assessment identified a number of risk exposures, which in combination could potentially have impacted on Southway's viability. The first concerned the delivery of its home improvement programme. Southway needed to deliver the final year of this five year programme on time and within budget. It has since achieved this and thereby met all of its promises to its tenants.

The second risk exposure related to compliance with loan covenants. The 2012 business plan indicated that 2013/14 was to be a challenging year in terms of complying with the lender's annual cash-flow covenant. Negotiation around the terms of the existing loan facility commenced in June 2013. By August 2013 new lending terms were in place and the restrictive cash-flow covenant had been removed. It has been replaced with an interest cover covenant which gives Southway more flexibility in terms of managing the delivery of its business plan.

Business plan reliance on gap funding receipts was also highlighted as a risk exposure. At transfer, Southway's business plan included gap funding receipts of up to a maximum of £34m (plus CPI inflation) over the first seven years of its operation. Southway is now in its final year of gap funding allocation and we understand that all eligible spend will be incurred by the year end, enabling the full entitlement to be claimed. This risk exposure has therefore been mitigated to a manageable level.

A further risk exposure related to the challenging cost inflation assumptions on which the 2012 business plan was based. As in the preceding version of the plan, the 2013 business plan makes challenging long-term assumptions with regard to the level of on-going cost inflation, which is assumed at RPI only across the board. However, following changes to some business plan assumptions, together with the impact of renegotiated covenants, the 2013 business plan has the capacity to absorb reasonable increases in cost inflation.

The regulator is satisfied that Southway's financial plans are consistent with, and support, its overall strategy. Financial forecasts indicate reasonable covenant headroom and there is ample security value in the stock base to support Southway's loan requirements..

The regulator's assessment of Southway's compliance with the governance element of the governance and financial viability standard remains unchanged. Based on evidence gained from contact with the board and executive and a review of board papers, the regulator has assurance that governance arrangements remain sufficient to adequately control the organisation to enable it to continue meeting its objectives.