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Welsh Government
Housing Policy - Regulation

Financial Viability Judgement

Merthyr Valleys Homes Limited – L150

February 2016

Financial Viability Judgement

The Welsh Ministers have powers under the Housing Act 1996 to regulate Registered Social Landlords in Wales, in relation to the provision of housing and matters relating to governance and financial management. Part 1 of the 1996 Act is amended by Part 2 of the Housing (Wales) Measure 2011 ("The Measure") and provides the Welsh Ministers with enhanced regulatory and intervention powers, concerning the provision of housing by Registered Social Landlords and the enforcement action that may be taken against them.

The Welsh Ministers are publishing this Financial Viability Judgement under section 35 of the Housing Act 1996.

This report sets out the Welsh Government's Financial Viability Judgement, which is designed to provide the Registered Social Landlords, its tenants, service users and other stakeholders with an understanding of the its financial viability.

The term 'Association' has been used throughout the report to refer to Registered Social Landlords (RSLs).

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Description of the Group

Merthyr Valleys Homes Limited (Merthyr Valleys Homes) is registered under the Co-operative and Community Benefit Societies Act 2014 and has charitable rules. It was created following a large scale voluntary transfer from Merthyr Tydfil County Borough Council in March 2009.

The Association owns and manages around 4,000 general needs homes, 200 sheltered homes and 34 commercial units. It also provides services to around 300 homeowners.

Merthyr Valleys Homes has reported meeting the requirement of the Welsh Housing Quality Standard in 2014. It has completed its first development of 21 one and two bedroom homes in 2015 and has a further 6 units due for completion within the next month.

For the year ending 31 March 2015, the Association's turnover was £15.7m (2014: £14.9m), its retained surplus was £2.5m (2014: £1.2m) and it employed an average of 179 staff (2014: 184).

Overall Conclusion

Our judgement of the Association's financial viability remains unchanged from last year.

As at January 2016, the judgement is: **Pass**

The Association has adequate resources to meet its current and forecasted future business and financial commitments.

This financial viability judgement is issued on the basis that the Association's 30 year financial plan complies with existing Welsh Government Policy, in particular the Policy for Social Housing Rents. Any changes to policy may necessitate a review of the findings of this judgement

Our judgement is based on the following findings:

The 30 year financial forecast has been prepared using a reasonable set of assumptions and it shows the Association continuing to meet its lenders' covenants.

The Association has adequate secured loan facilities in place in order to fund its forecasted spending on property maintenance and improvements, and it has sufficient income generating ability to service and repay such borrowings.

The Association's 30 year forecast shows that it should continue to operate within the lenders' covenants under reasonable scenario testing. The resetting of covenants annually, giving a 5% tolerance to the revised business plan places an onus on the Association to impose strict budgetary control over the current financial year. We are satisfied that the Association has controls in place to manage this.

Following a strategic decision to reduce void numbers, the Association is forecasting to be significantly overspent this year on its budget for void property maintenance. We are satisfied that this is affordable in 2015/16 due to savings having been made in other areas of the business. The Association needs to ensure that, going forward, it can deliver its plan to reduce void expenditure to ensure that it remains compliant with agreed funding covenants.

The Association reported the achievement of Welsh Housing Quality Standard by its target date of 2014. It has utilised stock condition survey information to inform the costs included in its 30 year forecast to continue to meet this standard.

The impact of the UK Government's Welfare Reforms, to date, has been within the expectations of the Association. Going forward it has assumed that there will be an increase in loss of rent from bad debts (from 1.5% in 2015/16 to 3.5% until 2017/18, before returning to 1.5% thereafter) as the UK Government introduces its Universal Credit provisions. We are satisfied that the assumptions made by the Association are reasonable given its current experience.

The Association receives £2.9m per year dowry funding from the Welsh Government. The Welsh Ministers currently intend to offer financial assistance for 30 years from the date of transfer (subject to the terms and conditions set out in the offer letter) and acknowledge that the Association's 30 year business plan is predicated on the assumption that financial assistance will continue to be offered for that period.

Sources of Information and regulatory activity

The following information is received from Associations and reviewed by the Welsh Government:

- Audited annual accounts, including the internal controls assurance statement;
- External auditors' management letter;
- 30 year financial forecasts;
- Quarterly management accounts;
- Private finance returns;
- 5 year business plans;
- Welfare reform data collection;
- Internal audit reports;
- Board papers, as requested;
- Financial and risk management information collected through regulatory engagement.

This is in addition to regulatory engagement with the Association.

Basis of Financial Viability Judgement

This judgement is based on information submitted by the Association and our accumulated knowledge and experience of the Association, its management and the housing association sector as a whole.

In preparing this report, the Welsh Ministers have relied on the information supplied by, or on behalf of, the Association. The Board and its Directors remain responsible for the completeness and accuracy of such information.

This report has been prepared for the Association as an opinion by the Regulator. It must not be relied upon by any other party or for any other purpose. Any other parties are responsible for making their own investigations or enquiries.

There are three categories of Financial Viability Judgement: "pass", "pass with closer regulatory monitoring", or "fail".

Where the judgement is "pass with closer regulatory monitoring", the Welsh Ministers are of the view that additional work and/or scrutiny, is required to provide stronger assurance on financial viability.

Where a judgement of "fail" applies, the Welsh Ministers will have already been working closely with the Association to address the underlying issues.

Annex 1: Glossary

Gearing is defined as the level of a company's debt, compared to its equity capital, usually expressed in percentage form. For Housing Associations, this is typically calculated as debt, divided by net assets and capital grants. Most Associations have gearing covenants that they need to comply with as part of their loan agreements.

Interest cover is defined as the ability of a company to pay its interest cost on its outstanding debt. This is typically calculated as earnings before interest, divided by interest payment. This is another common covenant that Associations need to comply with as part of their loan agreements.