Contents

Appraising the options for new affordable housing in Slough

Phase Two: Summary Report (FINAL)

PRIVATE AND CONFIDENTIAL

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1. Introduction and Methodology

1.1 Slough Borough Council have commissioned Savills to assist in supporting an appraisal of the options for the delivery of new affordable housing in Slough. Savills were appointed in late 2016 and we have worked closely with members, officers, residents and other stakeholders during the course of the project.

1.2 The project has been overseen by a Commissioning Consultative Group (CCG) comprising members of the cabinet, alongside a Residents Consultative Group (RCG) recruited specifically for the purpose of undertaking this work. A great deal of work has been undertaken in exploring the different options for the ownership, management and maintenance of Slough's existing council housing, and the options to deliver more affordable housing.

1.3 This report is intended to provide a summary of the work undertaken, the key financial and other factors that have arisen during the project and the conclusions which have been drawn about which options to take forward. Where appropriate, supporting material generated during the project is appended to this summary.

Methodology

1.4 The project has been overseen by the CCG and RCG, with input from specialist advisers:

- Savills - financial and investment advice, guidance and modelling
- Trowers and Hamlins - legal advice and guidance on the options
- Phil Morgan - independent tenant and resident adviser.

1.5 The project was run in two phases as follows.

1.6 Phase One:

- To review the current Housing Revenue Account (HRA) Business Plan, its capability to meet the future management and maintenance needs of the existing council housing stock, and the scope for the HRA to deliver new council housing over the long term
- To review alternative whole stock options for delivery of services and new homes, discounted Large Scale Voluntary Transfer to a housing association
- To identify all the various options that the Council could pursue in delivering new affordable homes, options to take forward into Phase Two
- To set objectives by the CCG's member representatives, and from the residents group, against which to appraise the options under review.

1.7 Phase One was undertaken between December 2016 and March 2017, and concluded with a summary report to the Council's Cabinet in April. The outcomes are further summarised below, the main headlines being that:

- The council is able to manage and maintain its existing council housing stock into the long term - and that there is no case for major stock transfer
- The HRA is constrained in the delivery of new homes and therefore Phase Two needed to concentrate on exploring the options to increase the amount of affordable housing.

1.8 Phase two has taken place from May 2017 to date. This summary report will form the basis of a report to Cabinet for review and decision.

1.9 Phase Two:

- To identify all the options for the delivery of new homes
- To test each of the options financially, in the context of deliverability and affordability within Slough, and test the extent to which each of the options is able to meet the needs for new affordable homes
- To appraise the options against the tests set by the CCG and RCG
- To identify and recommend those options to be taken forward into a delivery phase.

1.10 A key feature of the work undertaken has been the extent to which the Council is already embracing new models for delivery across a range of housing schemes and tenure types. To an extent, some of the options (for example, options to establish wholly owned companies to deliver new and different tenures within the local housing market) are already being pursued by the Council. This has made for a positive process in which the CCG, the residents and the Council have been open to new ideas. A review of these options was therefore incorporated into Phase Two.

1.11 At the same time, the Council asked Savills to undertake a detailed Asset Performance Evaluation (APE) of its existing council housing in order to identify where there may be opportunities for alternative use, or different approaches to make better use of assets. The outcomes from the APE have been integrated within Phase Two of the options appraisal in order to provide a more comprehensive overall set of outputs and conclusions for the Council to take forward.

1.12 The RCG/residents' consultative process was brought together in a Conference held on 28th October attended by over 60 tenants and leaseholders, alongside advisers and council officers and members. The Conference afforded an excellent opportunity to receive feedback from residents on the options appraisal process, and this report incorporates this feedback in its conclusions and recommendations.

2. Phase One Summary

1.1 The main outputs from Phase One are summarised below.

Review of HRA Business Plan

1.2 The Council has taken a cautious view towards some key assumptions, including adding real inflation to management costs, increasing rents at less than the Consumer Prices Index (CPI) from 2020 onwards and projecting significant reductions in stock through Right to Buy sales into the long term.

1.3 Given the pressure on the need for new housing of all types, the net stock loss forecast suggests that "doing nothing" is not really an option for the Council. Options need to be found to ensure that more affordable housing is available to meet needs now and in the future.

1.4 There is an ambitious but fundable new build and stock replacement programme over the long term – which includes £56m over the next 5 years.

1.5 The Council has however taken a more robust view towards some other assumptions, including making provision for real terms reductions to repairs expenditure (i.e. increasing at less than the rate of inflation) over the lifetime of the plan.

1.6 In overall terms, given the assumptions made and the cautionary approach, the business plan is financially viable. Whilst the plan is balanced in cash terms over 30 years (i.e. there are only minimum cash balances forecast for 30 years' time), there is significant borrowing headroom retained below the debt cap.

1.7 However, whilst viable overall, the business plan shows a net loss of stock of 12% over 30 years (Right to Buy sales of 20% of the current stock; 8% added back through new and replacement build).

1.8 There are a number of routes to delivering more homes in the HRA. A basket of loans with different maturity terms was taken out at cheap rates to pay for the HRA debt settlement in 2012. The business plan shows these loans being repaid as they become due. Adopting an alternative approach, in which loans are refinanced as they become due, could allow resources for further investment in new homes throughout the term of the plan.

1.9 Aligning expenditure and income inflation assumptions (that is, by assuming that income will increase by the same inflation rate as expenditure) might also release further resources for investment.

1.10 The application of assumptions within the HRA Business Plan is affected by the ongoing evolution of government policy towards social and affordable housing, with a series of announcements made during the course of phase two, which need to be taken into account in the business plan from April 2018. These are explored in more detail below.

Whole Stock Transfer

1.11 One possible option response which was modelled and discounted was a whole stock transfer to a newly created or existing housing association.

1.12 This was modelled on in phase one on the basis of the same basic assumptions contained within the HRA business plan (so that there is no favouring one option over any other). The main financial outputs are as follows.

1.13 An illustrative valuation of the housing stock is £77m. This would be the price paid by a purchasing housing association.

1.14 This compares to the HRA's current debt of £144m. This suggests that a transfer would leave a substantial overhang of debt that would not be paid off by the transfer-receipt and which would require financial support from government (to assist in debt write-off).

1.15 No government support is currently available.

1.16 There would be some significant diseconomies of scale for the General Fund, with an estimated impact on the General Fund of between £1-3m pa.

1.17 It is doubtful therefore that, even if there was a case for stock transfer, the Council could financially deliver such a transfer.

Options into Phase Two

1.18 Solutions for the delivery of new housing are therefore focused on council-owned and council-driven options in Phase Two. These were determined from the following approaches.

1. Maximising delivery in the HRA, subject to enabling stock to be built/acquired which remains affordable housing for the long-term.

2. Using existing and potentially new council-owned housing companies to build and acquire affordable and market housing.

3. Developing new approaches to raising public and private finance in joint ventures with housing associations, the private sector, and funding institutions.

4. Options which allow the delivery of a wider range of affordable tenures with greater flexibility in the future: for example intermediate rent (for example at the Slough Living Rent), rent-to-buy / rent-to-mortgage and shared ownership.

Councillor and Tenant Tests

1.19 At a joint workshop meeting of the CCG and RCG on 20th March 2017, members of the groups agreed a series of criteria against which to test the options going forward. These are referred to within this report as the Tenant Tests and the Councillor Tests.

1.20 The Tenant Tests were determined exclusively by members of the RCG:

- Maximise the transparency of any new approaches to delivery
- Security of tenure
- Rent and service charges levels to be affordable
- Avoiding subsidy of new properties from existing council housing.

1.21 The Councillor Tests are driven primarily from the Housing Strategy:

- Delivering new and affordable housing
- Sustaining our existing housing provision
- Meeting the need for housing in Slough
- Improving our offer for special needs and vulnerable groups
- Providing a way forward that is achievable.

1.22 In our advisory work to the CCG and RCG, we have been particularly mindful of the following key factors as provided for in the above:

- Adopting a definition of "affordable" which is linked to a view on earnings within Slough
- Reviewing options in the context of ensuring that there is no cross-subsidy required from the HRA, or from the housing service providing management and repairs services to council housing residents.

1.23 Section 10 below comprises the overall appraisal of options against these tests.

3. Phase Two: Overview of Options

Introduction

1.24 The CCG and RCG agreed to identify nine options (or approaches) for review within Phase Two. These are summarised in the diagram below.

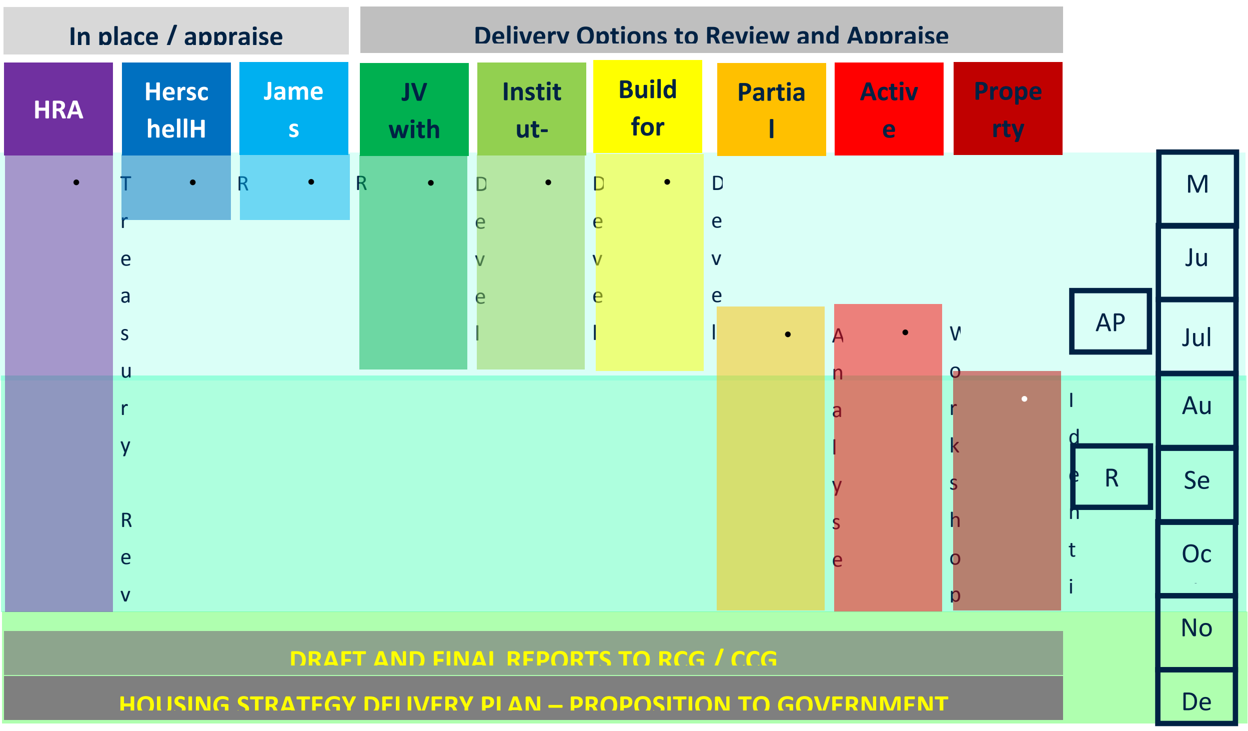
1.25 All of the options provide for additionality in terms of the existing base of social and affordable housing in the borough. Given that our review of some of the options was dependent on other work being undertaken in parallel to the Option Appraisal, specifically the Asset Performance Evaluation for the existing council housing stock, the review work was structured to take best advantage of the time available.

1.26 In general terms, the options divide into three groups:

- Existing delivery mechanisms in place at the Council
- New routes to public/private partnerships to lever in additional resources
- Options driven by the condition and nature of existing council housing stock.

Options Overview

1.27 The nine options are set out in the chart below along with an overview of the work undertaken and the timing followed.



1.28 Each of these options was considered in turn by the CCG and RCG.

Tower and Ashbourne site

1.29 So as to demonstrate a living example as to how the options review would impact upon the potential of developing '*New Social Housing by remodelling an existing HRA site*', during the course of the project, the ongoing potential for the redevelopment of the Tower House and Ashbourne House site near the town centre was identified as an opportunity to provide an exemplar of how new options might work for Slough. The existing scheme had two blocks with a total of 120 units, 104 of which were social-rent homes within the HRA and 16 of which were leaseholder flats.

1.30 Savills were appointed to undertake an initial Design Feasibility Study, in order to explore the potential number of homes that could be delivered on a redeveloped site. An initial presentation was made to a joint meeting of the Cabinet and CCG in September, setting out how it should be possible to remodel to a new site based around two blocks with a total of 195 homes.

1.31 In modelling the various options for new delivery using this as an exemplar, we have sought to ensure that:

- The whole site is modelled as affordable housing
- There is no net loss of affordable rented homes and that therefore a minimum of 104 homes would be at social rent, or other affordable rent level, with a particular focus on the Slough Living Rent which has been approved by the Council.

1.32 The modelling of the options in the context of a redeveloped Tower and Ashbourne site has enabled the CCG and RCG to focus on a "live" example of what the options that can deliver - with a clear impetus towards taking the scheme through the planning process during the early part of 2018.

Other considerations

1.33 Alongside the HRA and the two newly created housing companies, Slough also has an existing company (the Development Initiative for Slough Housing or DISH). This company was established several years ago to enable the development of new social housing outside the Housing Revenue Account, funded by private finance. It is understood that the lease term for the arrangements put in place are nearing the end of term.

1.34 Whilst DISH has not formed part of the Option Appraisal process run by the CCG and RCG, it is noted that this company will form part of the suite of vehicles in place for affordable housing for as long as it holds or leases affordable housing.

4. Review of existing options in place: Housing Revenue Account delivery

Introduction

1.35 During the course of this project, we have kept the options for HRA delivery of new council housing and wider affordable housing open for review.

1.36 Whilst there had been some hints of movement in the national policy environment towards council housing and funding for the HRA following the change of government in July 2016 (specifically the abandonment of the proposed Pay to Stay policy), the General Election held in June, during the course of this project, would appear to have had more of an impact on the future course of certain policy areas. The proposed capping of council rents to Local Housing Allowance has also now been abandoned.

1.37 There have been a series of announcements made by the Prime Minister and other ministers which suggest that there may be the scope to increase the delivery of new (or replacement) council housing. In particular:

- The announcement at the Conservative Party Conference, confirmed in the Autumn Budget, of an additional £2billion to be added to the Affordable Homes Programme with specific reference to social housing.
- The announcement in the Budget of a programme for the extension of borrowing limits by up to £1billion from 2019-2022 for HRAs in high-demand areas.
- Confirmation in the Budget of the opportunity to apply for loan funding for the regeneration of estates in high demand areas (a programme of up to £400million).

What is currently being delivered

1.38 The HRA Business Plan currently incorporates plans to deliver up to 200 new homes on small sites around the borough over the next 4-5 years. These sites are part of a large-scale overall development programme.

1.39 However the scope to deliver a large programme is fundamentally affected by two constraints:

- The operation of the Debt Cap - which prevents borrowing above a certain government-defined limit, irrespective of the viability of development opportunities. Whilst there is some headroom, the Council retains a buffer against future policy risk (which is financially sound practice). The amount of current headroom would, even if it was all committed up front, be insufficient to carry out the redevelopment of the Tower and Ashbourne site (for example, estimated cost minimum £30m).
- The ongoing challenges presented by the Right to Buy discount extensions made since 2012 - with sales now above 60 per year from the HRA.

What is changing (or has changed) during the appraisal process?

1.40 Whilst the signs are that the government post-election is showing more of a commitment towards funding the delivery of social housing (and therefore council housing), the change of government has meant delays in announcement on key policies, especially towards high value void/asset sales.

1.41 It therefore remains unclear as to whether the high value asset sales levy will be introduced at all, and if it is, on what timeframe and what shape the policy will finally take. Our central conclusion remains that, should the policy be introduced at any stage, this will provide an extremely significant challenge to the future operation of the HRA and it may be that the Council would need to reconsider its options at that point in the light of the actual proposed levy being raised.

1.42 However, given the legislative arrangements necessary for this policy to be implemented, coupled with constraints on the government's legislative timetable given the dominance of the issues around leaving the European Union, our view is that the Council can plan in the short to medium term without the need to provide for a large contingency for this policy.

1.43 The government has also announced the reversion to rent increases of up to CPI+1% per annum following the annual 1% rent cuts to 2020, for 5 years. This will provide councils and housing associations with some degree of income predictability over the medium term financial future. For Slough, this could mean that there are more resources within the HRA from 2020; there is the opportunity to revisit the capacity to deliver more homes when current programmes are complete.

1.44 As well as lobbying on the Debt Cap - which has led to the £1billion extension of borrowing limits announced in the Budget - the sector is pushing for the more flexible use of Right to Buy receipts. Following the Budget, there will be further details emerging on the basis for discussion with Government around funding bids, as well as the opportunity for bespoke deals and we will ensure that the Cabinet is appropriately briefed on the impact when this report is being discussed.

1.45 Conversely, locally, there has been further work on the investment needs of Broome House and Poplar House following the Grenfell Tower fire in June. This is likely to mean that, should the blocks be retained in their existing use, resources would need to be found in the HRA Capital Programme to meet these needs. In response, the Council is currently undertaking a more detailed feasibility study around the future options for the two sites, including whether there might be opportunities for redevelopment.

Prospects going forward

1.46 Our view is that the HRA is likely to best be seen as a contributor to small scale developments for the foreseeable future - as these are limited by Right to Buy and funding considerations.

1.47 Delivery of new social and affordable housing at scale is likely to require investment at levels that are unable to be currently sustained in the HRA without a successful substantial bid for additional headroom following the Budget.

1.48 However, the post-election policy environment has many uncertainties and the potential for Slough to engage with government/HCA regarding additional funding for social housing should be kept under review particularly given the announcements in the Budget.

5. Review of existing options in place: Sloughs' Housing Companies

Introduction

1.49 The Council has established Hershell Homes and James Elliman Homes, two wholly-owned subsidiary companies, in late 2016. Resources to finance the acquisition of stock by these two companies has been provided for within the capital and treasury management strategies of the Council.

1.50 With respect to the option appraisal, the CCG considered the extent to which these two companies could be utilised as a basis for the delivery of additional affordable housing. The primary reason for such a consideration is that the companies are already set-up and have a funding stream identified.

What is currently being delivered

1.51 Hershell homes is a company set up to acquire properties for market renting. It has not been established to deliver affordable housing, nor to develop new homes, although there are opportunities being explored to acquire new homes from developers upon completion. It is understood that 120 units have been identified for detailed appraisal and that this work on acquisitions is ongoing.

1.52 James Elliman Homes has been established to acquire and develop homes for use as temporary accommodation. As at the end of October 2017, Slough has c400 families in temporary accommodation, a significant number given the size of the borough.

1.53 Both companies have been provided with the opportunity to draw on borrowing lent from the Council's General Fund. Both companies have had their objectives set and governance arrangements put in place on the basis of the respective interventions in the market rented sector and in the provision of temporary accommodation.

1.54 They are therefore not able to be used for the development of new affordable housing without some consideration being given to amending the objectives and governance arrangements in place.

What is changing (or has changed) during the appraisal process?

1.55 There has been no specific changes to the plans of the companies since the option appraisal process began.

Prospects going forward

1.56 Both companies are able to be developed in their respective areas of the market place and their contribution assessed accordingly. They are not ideally suited for use for the development of affordable housing.

6. Review of new options: Joint Venture with Housing Association

Introduction

1.57 At the request of the CCG, senior directors and members of the Council have considered the opportunities to enter into a partnership arrangement with a large locally-based housing association (HA).

1.58 During the course of its work, the CCG has received presentations and information relating to joint ventures between local authorities with stock and housing associations that are in development. The external advisers presented examples of the type of partnerships that could be entered into, ranging from:

- Development Management arrangements whereby a HA provides skills, capacity and expertise alongside council funding (for example Epping Forest DC and East Thames Group)
- Three-way company between the Council, a Developer and a HA to bring forward redeveloped homes on existing council sites (for example Sheffield Housing Company)
- A 50:50 JV between council and large HA with the input of land and prudential borrowing funding from the council alongside funding and development capacity/expertise from the HA (for example Brighton & Hove City Council and Hyde Group), to deliver homes at Living Rent and for intermediate home ownership options.

What is currently being delivered

1.59 Whilst there are a number of high profile and relatively locally-based housing association groups (for example One Housing Group, A2 Dominion) with significant stock holdings in Slough, it was reported to the CCG that the Council's relationships with housing association partners were likely to require more work before consideration could realistically be given towards entering into a partnership or Joint Venture.

What is changing (or has changed) during the appraisal process?

1.60 No specific scheme or site options have yet come forward where this option might be explored in more detail or add value to other funding approaches.

Prospects going forward

1.61 Whilst this approach is not felt able to be developed for the Tower and Ashbourne site or any other sites/schemes at this stage, our view is that the Council should keep this option under review as new development and build programmes are delivered. There may be the opportunity to lever in additional resources and capacity in due course as the Council becomes more comfortable working in partnership with local associations.

7. Review of new options: Build for Sale Company for new affordable housing

Introduction

1.62 Hershell Homes and James Elliman Homes have both been identified as unsuitable to be used as vehicles to develop new affordable housing. At the same time, the Council is already a partner in a major Joint Venture with Morgan Sindell (Slough Urban Renewal) and this partnership is delivering at scale on multiple sites across the borough, including commercial and residential developments.

1.63 The CCG therefore considered the option to establish a further company, but one focused specifically around the development of new affordable housing for sale, or intermediate forms of affordable home ownership in which the sale of homes to residents would be the primary objective.

1.64 The models considered are being developed in other authorities and by the private sector, with a particular focus on Rent to Buy, Shared Ownership and Slough Living (affordable) rent as intermediate tenure options (the latter being a requirement in modelling the Tower and Ashbourne site redevelopment).

1.65 The CCG received a series of papers (appended to this report) exploring in detail the opportunity to provide Rent to Buy and Shared Ownership housing through a new company, with a particular focus on:

- The affordability of these intermediate options for different groups of people who might otherwise find it difficult to access full home ownership immediately.
- Identifying subsidy requirements for these tenure options, and also in the context of the potential need to re-provide for an element of social rented housing within a development (i.e. the Tower and Ashbourne site).

1.66 Appendix one comprises the paper presented to the CCG in August setting out our assessment of the affordability and deliverability of the Rent to Buy and Shared Ownership options. In summary:

- The Rent to Buy option would be based on letting a long-term tenancy (up to 20 years) at an affordable/Slough Living Rent, with some of the rent paid by the tenant being set aside to provide a gifted deposit towards purchase of the home at a specific point within the 20 year period. The Council would be responsible for management and maintenance until sale.
- The Shared Ownership option would be based on the "traditional" HA approach whereby a tranche of the home is sold on day one, rent paid on the balance retained by the landlord, with the resident having the option to staircase up to full ownership in the future. The resident would be responsible for maintenance.

In the Rent to Buy model, the subsidy to the resident would be provided through the letting at an affordable rent level with some of that contributing towards enabling future home ownership. The Shared Ownership model subsidises the resident through enabling part of the property to be bought at a time.

1.67 Under both of these tenure approaches, the company would be wholly owned by the Council, be funded via prudential borrowing from the Council, with sales proceeds being recycled either to repay debt or into the funding of new schemes.

1.68 Given increasing house prices and property values in Slough in the recent period, a trend set to continue into the future, both the Rent to Buy and Shared Ownership tenure models would deliver positive returns and/or profits to the company. These returns would be over and above the internal subsidisation of the residents in these schemes - in effect the subsidy of the residents would be "hidden" to the extent that the company would be profitable after taking into account these subsidies.

1.69 The principal considerations for the Council therefore are:

- Given the high values in Slough, can a tenure model be constructed which meets the test of affordability to residents (defined as between 30%-40% of take home pay spent on housing costs)?
- To what extent is the Council comfortable subsidising a specific group of residents to become home owners in the borough, by how much and for how long?

These considerations are discussed further below.

<u>What is currently being delivered</u>

1.70 There is nothing in place currently, though there are some examples of shared ownership in Slough offered by housing associations.

<u>What is changing (or has changed) during the appraisal process?</u>

1.71 The coming forward of the Tower and Ashbourne site to be used as an “exemplar” site has allowed the comparison of new intermediate models in the context of replacement of 104 former social rented homes plus a significant increase in property numbers to 195. It has also provided some explicit estimates of valuations of new homes on the redeveloped site - in order to finalise the modelling for rent to buy and shared ownership.

1.72 It is noted also that the development of a partnership vehicle with Osborne’s (see below) has placed a new Council-JV vehicle into focus - alongside the option for a new 100% owned vehicle. The benefit of this development is primarily around the use of One-for-One Right to Buy receipts - which are able to be deployed to fund schemes operated by the JV, but not in a company in which the Council has ultimate control.

<u>Prospects going forward</u>

1.73 In respect of the Rent to Buy approach:

- The Tower and Ashbourne replacement valuations are somewhat higher than the valuations modelled earlier for the CCG (and which form the basis for appendix one)
- The need for rent set-aside (towards a deposit) would typically be above 50%

- The timeframe over which the rent set-aside would need to operate could be quite lengthy (perhaps over 15 years) in order to build up the deposit necessary - with house prices increasing in the meantime
- In all probability, the scheme could only operate with the objective for the tenant to achieve a shared equity position within the property (Rent to Shared-Equity, rather than Rent-to-Buy).

Taken together, these make the delivery of Rent to Buy a challenge in Slough, primarily driven by the high values.

1.74 In respect of Shared Ownership:

- Given that the initial tranche sold could be as low as 25%, or even 20%, and given no requirement to staircase over a particular time, initial occupation of the home could be quite deliverable
- The traditional HA approach with rent level of 2.75% per annum of net retained equity does make for less affordability to the resident, taking rents and likely mortgage costs together
- However, the Council / Company could determine to adopt a different rent policy to the HA standard, perhaps offering rent at 2.5% or even 2.25% of net retained equity
- Affordability is likely to be lower compared to the Slough Living Rent, but the resident would be building up net worth in the part of the property they own.

Taking these together, therefore, it is possible for the Council to develop a model for a Shared Ownership product for Slough, delivered through a subsidiary company or partnership, with further consideration given to the terms and rent levels within the scheme.

1.75 If, as is required for the Tower and Ashbourne site, there is a need for replacement social housing alongside Shared Ownership, it is noted that delivery through a partnership in which the Council did not have a majority control would enable investment of Right to Buy receipts to assist in financing the social housing.

8. Review of new options: Institutional Investment

Introduction

1.76 A key feature of the investment and funding landscape over recent years has been the development of new forms of private finance available for investment into affordable rented housing. Investors such as Pension Funds and Institutions have large amounts of capital available to deploy into physical assets at relatively lower returns to match their liabilities towards pensioners.

1.77 The nature of this type of investment is that it is particularly suited to long-term affordable rented homes. Whilst it is not incompatible with Rent to Buy and Shared Ownership models, this would not be the preference of institutions.

1.78 The CCG has therefore considered how an institutional/private finance deal might work at Slough Living Rent – using a standard “leaseback” model where the council runs the properties, pays an index-linked lease cost to the investor, with the properties reverting to the Council after 30 years.

1.79 It is highlighted that other approaches could be used, in particular approaches where rent and occupancy risk is shared by the Council and investor. However, for modelling purposes, we have focused on the traditional leaseback approach. Appendix Two comprises the summary paper discussed by the CCG at its meeting on 3rd August.

1.80 In summary, the approach would be to offer all homes on a site at affordable rent, with the investor providing the funding up-front for the development, retaining the freehold for the term. The Council, through a subsidiary company established for the purpose, would take a long lease on the development, paying an index-linked lease rent, retaining any excess rents charged to the tenants for long-term management and maintenance of the stock.

1.81 Following the initial design layout and information on values for the Tower and Ashbourne site, our central modelling case is based on rents at the Slough Living Rent (approximately 70% of market rent - £820/month), charged on homes that have cost £170k to develop (all-in), with rents rising at CPI only and returns to the investor starting at 4.0% per annum. This combination of factors would allow the Council to retain sufficient resources from the gross rents to meet the lease payments to the investor and pay for all the management and maintenance needs of the homes over 30 years.

1.82 In practice, we might expect that, through some form of competitive approach, the Council could achieve better terms than those modelled above (for example a lower return requirement over a shorter term).

1.83 As for the other intermediate options in respect of the redevelopment of Tower and Ashbourne House, we have also identified subsidy requirements depending on extent of social rented housing within a development should not all units be deliverable at Slough Living Rent.

1.84 A final point to make is that the liabilities towards the lease would be recognised in the Council's balance sheet. Though no funding would be required directly (through borrowing for example), there is an impact on the balance sheet that would need to be provided for. In practice, this could be a positive and complementary approach for the Council given the extent of the borrowing commitments being provided to Hershell Homes and James Elliman Homes.

What is currently being delivered

1.85 There is nothing in place currently, though it is understood that the Council has had some preliminary discussions with some institutions regarding other development sites in the borough.

What is changing (or has changed) during the appraisal process?

1.86 As for the other options, the coming forward of the Tower and Ashbourne site to be used as an "exemplar" site has allowed the comparison of new intermediate models in the context of replacement of 104 former social rented homes plus a significant increase in property numbers to 195. It has also therefore provided the opportunity to model the interplay between different rent levels and numbers at each level, in particular: 104 at social rent, 91 at Slough Living Rent, up to all 195 at Slough Living Rent.

Prospects going forward

1.87 Institutional finance is best suited to 100% affordable rented homes over the long term – if some social rented homes are included, this would mean some need for subsidy.

1.88 The Tower and Ashbourne site is a good size for initial investment (c£30million) – with the prospect of more investment available across the borough on similarly sized (or larger) sites. The Council could keep the option open to deliver long term rented homes across a range of sites.

1.89 Interest from investors in delivering affordable housing in Slough is likely to be very strong, given the underlying positive factors around demand, need and value. We could expect to achieve significant value within this development if offered to investors to present their terms. Achievement of the best terms would also include some form of under-write or guarantee provided by the Council.

1.90 The share of risks and rewards in such a scheme should be carefully considered. The traditional leaseback-type scheme can be identified as risky to the provider in that the Council is "on the hook" for lease rent payments irrespective of how much rent is actually collected from tenants. Whilst demand and need in Slough is currently very high, the Council would need to satisfy itself that demand into the future would be sustained. Conversely, it may not cost the Council the full amount of rent retained for management to actually manage the homes. It may also be possible to enter into dialogue with an investor to achieve a different share of risks.

1.91 Taken together, therefore, we believe that the redevelopment of the Tower and Ashbourne site as an exemplar with an institutional investor is an option the Council could pursue.

2 Review of options arising from current asset performance

Asset Performance Evaluation and Active Asset Management

2.1 In parallel with the Option Appraisal Phase Two project, work has been undertaken to carry out an Asset Performance Evaluation (APE) of the existing council housing stock. The APE process is focused on developing an objective measure of the performance of assets in their current use, by analysing the financial performance through income and expenditure cashflows for each individual property, aggregated to Asset Groups (geographical and by property archetype) and comparing these to measures of sustainability developed in conjunction with council officers.

2.2 The APE modelling has been the subject of an extensive and detailed process of iteration and feedback with a working group of officers across a range of disciplines within the housing and repairs service.

2.3 It is not necessary to repeat the detail within this report. However, the CCG was able to review the high level outputs from the APE project and come to a view on the future operation of Active Asset Management within the council housing stock.

2.4 These conclusions have focused on the following.

There are examples of relatively "poor" financial performance within the following:

- Poplar and Broom House - driven by the need for re-cladding
- Bedsit bungalows driven by low rents, higher than average voids and also high investment need.

There are examples of "marginal" financial performance within the following:

- Properties in age restricted blocks.

In respect of management area/geography:

- Stock is of marginal value in the Upton and Town Centre areas
- 50% of the homes in Kederminster have poor or marginal financial performance
- The stock in the south generally performs less well than the stock in the north of the borough.

2.5 Savills' approach to the ongoing use of APE modelling is to generate an approach towards local "option appraisal" driven by factors such as those set out above. The APE outputs are not deterministic and there is always the need to conduct further exploration of local options.

2.6 For Slough, the triggers for initial option appraisal could be:

- Those properties with poor financial value
- Prioritising 331 properties where values decline over the next 5 years indicating that investment should be reviewed as to its impact on future performance.

2.7 The option appraisal approach is central to Active Asset Management. In addition, we have identified and mapped possible opportunities where there may be vacant land/garage sites next to areas of higher demand, higher rents or better long-term value. The Council will be able to use this mapping and approach to cross-reference where assets might be both poor performing (in relative terms) and in areas where redevelopment might be possible, alongside less obvious opportunities where assets perform well in current use but where there might be opportunities to increase densities or changes to affordable mixes through redevelopment.

2.8 Active Asset Management should become an ongoing and annual process of review and analysis for the Council, as part of a dynamic approach in which the Council is constantly reviewing its options to increase the supply of affordable housing.

Partial Stock Transfer

2.9 The generic option to pursue a locally based stock transfer to a social housing provider, whether created by the Council or an existing provider, was identified as the possible outcome from the Asset Performance Evaluation exercise, should there be some assets or groups of properties that are in need of extensive investment unaffordable to the HRA, or where full funding for the capital programme within the HRA might not be achievable.

Housing Management / Property Services options

2.10 Within Phase One of the option appraisal, a series of options around alternative management provision options were identified and discussed at a high level, These included (for example), outsourcing services to a third party provider (for example Cheshire West and Chester Council). The CCG concluded that at that time there was no strong case for considering these options further given the focus on new development and supply of affordable housing.

2.11 During Phase Two, the conclusion of the Repairs, Maintenance and Investment partnership with Osborne's highlighted that there may be options around the development of a Partnering Venture approach with the contractor to explore the delivery of a wider set of services across the council and into the private sector. The RMI bidding process required Osborne's to provide for the establishment of a Partnering Venture with the Council for such additional services.

2.12 The Council has subsequently agreed to enter into a trading partnership with Osborne's in which it holds a 49% stake. This structure allows the investment of Right to Buy receipts should the partnership ever be utilised for the provision of new affordable housing. The partnership has already begun to actively consider the provision of Modular Housing to assist in meeting temporary accommodation needs.

2.13 The CCG has therefore been able to conclude that, alongside options to develop new wholly-owned companies for the development of affordable and intermediate housing, there may be the option to utilise this new partnership in order to facilitate the delivery of new homes. The Council should keep the scope for delivery through these various mechanisms under review.

3 The Tenant and Councillor tests

3.1 As referenced in section 2 above, the options have been compared to the two sets of Tests set by the Tenants (RCG) and Councillors (on the CCG). The outputs are set out below.

Tenant Tests

3.2 For ease of reference, these are presented in two tables.

Tenant Tests: HRA and build for affordable home ownership;

	Housing Revenue Account	**Build for Rent to Buy**	**Build for Shared Ownership**
Transparency of new approaches	As now.	Company to be set up. Some transparency through council ownership and control over directors Landlord services provided by the Council.	Two models: company or HRA. If company some transparency through council ownership and control over directors. If Council arrangements as now. Landlord services provided by the Council.
Security of tenure	Flexible for new tenants, lifetime for existing.	Assured tenancy at affordable/ living rents	N/A
Rent	Social rent. HRA also able to deliver shared ownership	Slough Living Rent (70%)	Above Slough Living Rent but below market.
Service Charges (Leaseholder)	Existing arrangements would apply.	Only applies if equity option taken up so choice by tenant at that time. Existing arrangements would apply.	Subject to service charges. Should be known at time of purchase. Existing arrangements would apply.
Avoiding subsidy of new properties from HRA	Need to make sure that new build in the HRA is viable in itself	Outside HRA. Some benefit as management fees charged.	No direct impact - may use RTB receipts if otherwise would be paid to government

Tenant Tests: Institutional investment, LA/HA JV, Asset Management and management

	Institutional Investment	LA/JV Partnership Options	Active Asset Management	Trading/Property Management company
Transparency of new approaches	Company to be set up. Some transparency through council ownership and control over directors but limited. Landlord services provided by the Council.	Company to be set up. Some transparency through council ownership and control over directors but limited. Landlord services provided by the Council.	Asset Performance Evaluation process should lead to resident engagement within locally-based option appraisals	Landlord services provided by the Council.
Security of tenure	Assured tenancy at affordable/ living rents	Assured tenancy at affordable/ living rents	Flexible for new tenants, lifetime for existing.	Depends on tenure delivered and managed
Rent	Slough Living Rent (70%) as base case - but could be higher or lower rents depending on commercial terms	Slough Living Rent (70%)	Replacement homes for redeveloped sites could be at a range of rent levels	Depends on tenure delivered and managed
Service Charges (Leaseholder)	Subject to service charges. Should be known at time of purchase. Existing arrangements would apply.	Existing arrangements would apply.	Existing arrangements would apply.	Depends on tenure delivered and managed
Avoiding subsidy of new properties from HRA	Should be self funding although risk if rent collected is less than management costs.	Should be self-standing.	Active asset management seeks to eliminate subsidy of poorly performing properties	Allows investment of RTB receipts if council has a minority share

Councillor Tests

3.3 The tests set by councillors are repeated below. To an extent, the first three of these are "givens" in that all options are designed explicitly to deliver new, affordable housing in Slough, and the outcome of Phase One explicitly identified that the options considered have been in the context that the sustainability of the HRA stock is a pre-requisite.

1 Delivering new and affordable housing
2 Sustaining our existing housing provision
3 Meeting the need for housing in Slough
4 Improving our offer for special needs and vulnerable groups
5 Providing a way forward that is achievable.

3.4 It is in the fourth and fifth criteria that the options differ. This is discussed below.

3.5 In respect of the offer for special needs, vulnerable groups and supported housing in general, the CCG and RCG have tended to focus the attention of the review work towards the delivery of "generic" affordable housing. Our view of the applicability of each of the options towards supported housing is summarised as:

- The HRA is able to deliver new supported housing subject to the funding constraints within the business plan. Supported housing delivery in the HRA does not attract the Right to Buy which is an advantage compared to general needs housing. The main constraint will be related to funding to the Debt Cap, and the majority of HRA small-site development would not be suited to supported housing delivery (which tends to require some scale).
- Rent to Buy through a company would not be suited to supported housing.
- Shared Ownership through a company could be suited to supported housing in respect of "downsizers" (people looking to sell larger homes and "downsize" to a smaller apartment in a supported scheme).
- Institutional Investment is well suited to investment in supported housing - in fact the majority of institutional investment to date with housing associations has been focused into this type of scheme (either existing provision to release capital for the HA, or for new provision).
- Active Asset Management opportunities to deliver new supported housing are part of the Option Appraisal process.

3.6 In respect of the achievability of options, this has been discussed throughout the report and is summarised below:

- The HRA is already achieving new development on smaller sites but is unable to deliver new council housing at scale without a change to funding rules; the Right to Buy also applies to general needs housing developed on any scale.
- Rent to Buy through a company is not achievable on the measures set out within the appraisal.
- Shared Ownership through a company is achievable and can form part of the offer to residents.
- Institutional Investment is likely to be achievable for sites of appropriate size and scale.
- Active Asset Management opportunities to deliver new housing are part of the Option Appraisal process.

4 Conclusions and Recommendations

4.1 The foregoing summary has set out the phasing, options, key factors and findings from the work undertaken by the CCG and the RCG.

4.2 Feedback from the Residents Conference held on 28th October has been provided to the Council within a separate report. In the context of this Option Appraisal, we note the general degree of support from the conference towards pursuing an institutional investment option with a rather more lukewarm approach towards shared ownership. We note also the focus of all delegates on the need for suitable quality and space standards for all new developments and that the initial proposals for the redevelopment of Tower and Ashbourne would meet such a need.

4.3 The overall conclusions and recommendations are for the Council to.

1. Following the forthcoming Budget announcement, review whether to apply for additional funding from the Government/Homes and Communities Agency[1]. This could focus on a bid for additional borrowing headroom and/or loan funding for remodelling.

2. Continue to pursue opportunities for new delivery through Hershell Homes and James Elliman Homes recognising that the objectives set for these companies primarily relate to the acquisition of market rented housing and temporary accommodation

3. Keep open the option to discuss partnerships with housing associations.

4. Develop a bespoke model for Shared Ownership in Slough, offered initially on a limited basis to test demand.

5. Pursue an option to raise private finance through pension fund or institutional investment to deliver new affordable rented housing in the borough, and specifically for the proposed redevelopment of the Tower and Ashbourne site (subject to planning permission).

6. Continue to investigate options for the optimal reinvestment of One-for-One Right to Buy receipts into affordable housing in the borough, in the light of the establishment of the establishment of the Council's Partnership Venture with Osborne's.

7. Develop an Active Asset Management Strategy based on the analysis within the Asset Performance Evaluation - to be updated annually.

8. Within the Asset Management Strategy, appraise the options for those assets which are under-performing relative to the rest of the stock with a view to remodelling, redeveloping or re-providing in the context of increasing supply.

[1] *A briefing will be provided on the implications of the Budget alongside this report if required.*

Appendix One: CCG Paper 3 August 2017 re Intermediate Ownership Options

Slough BC Housing Delivery Options

Build for intermediate home ownership options: updated example scoping

Introduction

At its last meeting, CCG received an initial paper scoping out the options for intermediate home ownership, covering the option to establish a build-for-sale company to deliver Affordable Rent to Buy and/or Shared Ownership tenure types to enable paths to affordable home ownership for suitable recipients.

The Rent to Buy model is based on setting rents at an affordable (Living Rent) level and setting aside some of the income received into a "virtual" deposit which is gifted as cashback at sale.

This paper provides an update as follows:

1. <u>Refine modelling for market values and rents in the light of further work undertaken on the local housing market</u>
   Average values for 2-bed units modelled at £300,000 opening open market value and average market rents modelled at £1,000 per month. The impact is to reduce affordability, with the option to retain an equity share on sale (therefore, product becomes more "rent to equity share") able to support the affordability gap.

2. <u>Extend rent to buy qualification terms to between 5 and 15 years</u>
   This has the effect of increasing the amount of virtual deposit over an extended period so that homes become more affordable as time goes on.

3. <u>Model an outline business plan for a company based on the use of the Tower/Ashbourne site for these tenure types (135 units - pending more detailed development appraisal and design work at this site being undertaken in parallel)</u>
   Capital costs have been modelled at c£20m financed by the Council with 65% of the funding treated as debt (i.e. company paying interest to the council) and 35% treated as equity (effectively council cash left in the company until such time as properties are sold). There is no assumption of land value at transfer (from HRA to company), however the model generates surpluses as future sales proceed.

The overall conclusion remains that a Rent to Buy model could be developed in Slough, delivered via a company, but with the proviso that it would either take many years (15+) for an occupier to have earned sufficient "deposit" for 100% purchase, or that the Council could offer a "Rent to Shared Equity" alternative at (say) 70-80%.

Conversely, conventional Shared Ownership models stretch affordability criteria which could make this option less attractive (on standard terms), particularly if salaries approach £40k and above.

Rent to Buy

Affordability for the tenant/occupier

The table below illustrates how the rent to buy model could work for three salary points - £30k, £40k and a nurse's median salary in Slough of £34,589. Definition of "Affordability" is again deemed to be 30% of take home pay and close to where a Slough Living Rent might therefore be pitched. The %age of rent set aside for a virtual deposit is 60%.

The modelling makes assumptions about inflation (2% for CPI, house prices and income), and shows how much deposit could be built over 5, 10 and 15 years, and what purchasing power might therefore be available at each of those points. The table also shows affordability in the context of what mortgage could be afforded (at 5% interest only cost).

Description	£30k salary	Nurse Med	£40k salary
Salary	30,000	34,589	40,000
Annual take home pay	23,676	26,796	30,288
Monthly take home pay	1,973	2,233	2,524
0.3 of monthly take home	592	670	757
Average market rent	1,000	1,000	1,000
Living rent as % of market	59%	67%	76%
Mortgage capability (5%) 5 yr	153,766	174,029	196,708
Virtual deposit 5 years	22,178	25,101	28,372
Purchase power 5 years	175,944	199,130	225,080
%age equity at O M Value	54%	61%	69%
Mortgage capability (5%) 10 yr	169,770	192,142	217,182
Virtual deposit 10 years	46,664	52,814	59,696
Purchase power 10 years	216,434	244,956	276,878
%age equity at O M Value	60%	68%	77%
Mortgage capability (5%) 15 yr	187,440	212,141	239,786
Virtual deposit 15 years	73,699	83,411	94,281
Purchase power 15 years	261,139	295,552	334,067
%age equity at O M Value	66%	75%	84%

The table shows that purchase affordability increases over time as the virtual deposit is built up. The level of subsidy being offered is both in the rent discounted to market levels (for the median example rents are 2/3rds of market) and in the offering of a discount at purchase. Salaries would need to be higher than £40k to approach being able to purchase outright.

Company Financial Plan

We have assumed £150k per unit build cost for 135 units - an investment of £20.25m. This could be funded 100% by the Council investing resources into a company, with 65% (£13.16m) deemed to be debt attracting interest at 4.5% and 35% (£7.09m) deemed to be equity left in by the Council as shareholder.

Management costs are £1,000 per unit per annum. Allowance for taxation has been made (VAT and Corporation Tax). However, no land value at transfer has been assumed. Demolition would be covered by the HRA capital programme.

We have modelled the financial factors for each of 5, 10 and 15 years to highlight the main outputs (were all occupants to exercise their rent to buy option at each of these points).
When properties are sold to the occupier, the prevailing market value is reduced by the virtual deposit (gifted as cashback), the equity retained in the property as the tenant is unable to afford the full price, and a small element of sales costs. Cash proceeds then repay the debt lent from the Council leaving a cash surplus for the company against the equity injected by the Council as shareholder.

The table shows the main outputs assuming 135 x Nurse-Median-Salary occupants.

Description	5 years £m	10 years £m	15 years £m
Capital cost	20.3	20.3	20.3
Equity	7.1	7.1	7.1
Debt	13.2	13.2	13.2
Gross Open Market Values	43.8	48.4	53.4
Less virtual deposit	-3.4	-7.1	-11.3
Retained equity	-17.0	-15.3	-13.5
Sales proceeds gross	23.4	25.9	28.6
Sales proceeds net of costs	23.0	25.4	28.1
Debt repaid	-13.2	-13.2	-13.2
Cash surplus vs equity	9.8	12.2	14.9
Retained property equity	17.0	15.3	13.5
Net rents received	1.5	3.3	5.7
Shareholder equity return	14%	11%	10%

The table shows that if the tenants all bought on these terms after 10 years, the company's initial outlay of £20.3m would be recouped through selling the homes for net proceeds of £25.4m, with the company receiving £3.3m of net rent income in the 10 year period.

Note also that the company would almost certainly be able to employ landlord services, paying fees for management and maintenance into the HRA.

The table therefore shows that surpluses can be generated from net sales, even after the deposits have been gifted, delivering strong returns for the Council as investor. (Note also that the Council would receive an on-lending premium on the debt lent into the company - not included in the table above).

These returns would be added to if, at any point, the occupier were to sell the property as the company would then receive a share based on retained equity in the property.

There would therefore be the opportunity to develop a view about land value between the HRA and the company at the outset.

Alternative offer through the HRA?

For illustrative purposes, we have also modelled the scheme as if it were provided within the HRA. This is illustrative as there would need to be legislative and tenancy rule changes in order to allow such a product to be offered within the HRA - however a form of 15 year rent to buy tenure type did appear in the government's recent election manifesto.

There would be no material difference as far as the tenant/occupant is concerned. Variation from the company model could be as follows:

- All £150m capital costs could be borrowed as HRA borrowing - providing within the debt cap; interest costs would be at the average HRA rate - c3.5%
- No additional management cost would be incurred.

Sales at 5 years would yield a net £2.8m sales surplus to the HRA added to £2.1m of net rents in the intervening period.

Sales at 10 years would yield a net £5.2m sales surplus to the HRA added to £4.8m of net rents in the intervening period.

Sales at 15 years would yield a net £7.8m sales surplus to the HRA added to £8.1m of net rents in the intervening period.

Summary

The Council is potentially able to offer an Affordable Rent to Buy product on terms similar to those set out above. The optimal returns would be via a company model which is deliverable subject to getting land from the HRA into the company. Given market values in Slough, it is likely that this would be a Rent to Shared Equity model with perhaps a target of 70-80% equity share to the occupant.
Delivery through the HRA would only be an option only with legislative change.

Shared ownership

Shared ownership on traditional terms, which involve the sale of an initial tranche of equity on day one, with rent paid at 2.75% of retained equity value (subject to RPI increases annually), remains an option for the council, either through the HRA or through a company.

The table below shows affordability for each of the salary points set out above. Based on a 25% initial tranche purchase (with assumed mortgage at 5% interest only), the costs as a proportion of take home pay vary from 42% for a £30k salary, 37% at the nurse-median-salary, to 33% for a £40k salary.

Description	£30k salary	Nurse Med	£40k salary
Salary	30,000	34,589	40,000
Annual take home pay	23,676	26,796	30,288
Monthly take home pay	1,973	2,233	2,524
0.3 of monthly take home	592	670	757
Average market rent	1,000	1,000	1,000
Living rent as % of market	59%	67%	76%
Initial tranche purchase	25%	25%	25%
Initial tranche capital	75,000	75,000	75,000
Mortage cost @ 5%	3,750	3,750	3,750
Retained equity	75%	75%	75%
Retained equity capital	225,000	225,000	225,000
Rent on retained equity (2.75%)	6,188	6,188	6,188
Annual cost to occupant	9,938	9,938	9,938
%ge of take home pay	42%	37%	33%

In future years, as the rent moves with RPI, which tends to be higher than CPI or salary growth, it is in the interests of the occupier to staircase regularly to keep costs affordable. This makes the product most effective for those who might expect their earning power to increase as their career develops.
For the Council (or company), the initial tranche sale reduces the amount required to be financed from debt/borrowing and running costs are low as repairing responsibility passes to the occupant. This would make for an effective and financially viable plan.

Steve Partridge, Savills August 2017

Appendix Two: CCG Paper 3 August 2017 re Institutional Investment

Slough BC Housing Delivery Options

Institutional Investment: exemplar analysis introduction

CCG received a summary introductory paper covering the basic features of institutional investment into affordable housing via a leaseback mechanism at its last meeting. Following that meeting, we have worked with officers to develop exemplar to work in sufficient scale to illustrate how such a scheme might look for Slough.

This paper therefore offers an updated summary of the main features for the CCG and an illustration of a possible scheme across three areas with three levels of affordable/intermediate rent.

As set out previously, the primary interest for institutional investors is long term, stable, index-linked income - this therefore fits most closely with the provision of long-term affordable rented schemes. We also covered at the last meeting why the sale of existing stock in this structure would be unlikely to work.

The model could therefore be based around the funding of newly built stock by an institutional investor or pension fund with the council leasing the stock back through a long-term Fully Repairing and Insuring (FRI) lease. The key features of this type of lease are as follows:

- Long term - typically beyond 30 years - modelled at 30 years below.
- Large-scale - we have modelled three possible schemes (Tower/Asbourne included) totalling 360 properties
- Index linked lease payments from the Council to the investor rising with CPI
- No break clauses but with the ability to substitute stock
- Tenancies as social/affordable - with the Council as the landlord
- All tenancy related costs are paid by the Council - management, repairs, void loss, bad debts
- Nil reversion - properties revert to the Council after 30 years for a nominal sum (£1).

The main financial factor required by investors is the "Net Yield" - the net rent divided by the amount of their investment. Our estimate of a 30-year, CPI-linked structure would be for a Net Initial Yield of 4.00%. For every £10m invested, the investor would look for £400,000 per year from the Council, which would rise with inflation irrespective of the costs and occupancy levels of the homes.

Exemplar analysis

We have modelled a possible 360 unit deal across three sites, some of which would require re-provision of social rented homes. We have adopted three "price points" for rent levels, to illustrate a possible combination of tenure types.

The rents charged to tenants would therefore be at three levels, perhaps depending on their circumstances, broadly representing "half-market or social rents", two-thirds market (per a £30-35k salary Living Rent level) and 80% of market rent (per a £40-45k salary Living rent level). The amount retained by the Council to run the stock would be 25% of the gross rents.

The main financial inputs are summarised in the table below. The table shows "price points" for rents at £500/month, £670/month and £800/month with the consequent "purchase price" able to be provided by an investor: £105k, £142k and £169k respectively.

	Half Mkt	2/3 Mkt	80% Mkt
Monthly rent level	500	670	800
Proportion of take home	0.36	0.34	0.32
Average market rent	1,000	1,000	1,000
Rent as % of market	50%	67%	80%
Annual rent	6,000	8,040	9,600
Gross-Net	75%	75%	75%
Net rent to investor	4,500	6,030	7,200
Retained by SBC	1,500	2,010	2,400
Target Net Initial Yield	4.00%	4.00%	4.00%
Gross purchase price / unit	112,500	150,750	180,000
Net purchase price (94%) pu	105,750	141,705	169,200

As an illustration, if there were to be 120 units provision at each price point (total 360), the total investment would be as set out in the table below.

	Half Mkt	**2/3 Mkt**	**80% Mkt**	**Total**
Gross purchase price	112,500	150,750	180,000	
Net purchase price (94%)	105,750	141,705	169,200	
Total number of units	120	120	120	**360**
Gross invested by investor	13,500	18,090	21,600	**53,190**
Net invested - after costs	12,690	17,005	20,305	**50,000**
Opening gross rents	720	965	1,152	**2,837**
Opening net rents	540	724	864	**2,128**
Retained by SBC	180	241	288	**709**

The table shows that with rents at these levels, the investor might be able to afford to invest £53m in developing the properties - £50m after deal costs and taxes.

In the first full year, gross rents would be £2.8m and the lease payment to the investor £2.1m, the Council retaining £709k to manage and maintain the properties.

Over time, the £2.1m net lease payment would rise with inflation, and this would not be changeable. Providing the properties are occupied with tenants paying rent, and the costs can be contained within the amount retained by the Council, the scheme would be viable.

The chief risk is that the properties are unable to be let to tenants at rents sufficient to pay the lease rental and the running costs - an example might be if demand was to fall so that the Council had to reduce rents in order to let the properties. They would not be able to reduce the payment to the investor. The chief risk mitigation is that the properties revert to Council ownership for £1 after 30 years.

The model implies that the development cost would be c£139k/unit. If it was to cost more to develop the sites, one or both of the following would be necessary:

- A higher proportion of properties at the higher rent levels
- The investor accepting a lower lease rental - perhaps 3.75% initial yield.

Tower and Ashbourne site only

Were a scheme focus on the Tower/Ashbourne site only, this would be for 135 units (subject to the work being undertaken on design options) split 45 each for the three price points: 45 at social rent, 45 at Living Rent, 45 at 80% market.

The equivalent investment that could be afforded would be £18.75m.

From an investor perspective, the likelihood is that they would be looking for the opportunity to deploy substantially more funds over time.

Some issues

Investment of £50m could not be provided for within the HRA business plan under current rules given the debt cap. An investor would almost certainly be able to provide the funds for development, given planning permission in place and a developer/contractor on board.

Funds provided for in this way are likely to be competitive compared to other private finance sources. Alternatively, the Council could finance development through prudential borrowing in the General Fund and sell the scheme to the investor at completion.

Since this is a Finance Lease, the lease amount would count against the Council's capital financing totals - so there would need to be a separate vehicle set up outside the HRA.

Summary

Interest from institutional investors in affordable rented stock in Slough would likely be very strong. All the underlying factors are positive: demand, rising rents and values, a Council management provider in place.

The sale of existing stock and leasing back should be ruled out. There is the opportunity to seek investment at scale on these terms to finance new developments or re-developed estates.

Steve Partridge, Savills August 2017

Appendix Three: Right to Buy receipts: updated position / requirement to spend

A summary of the current Right to Buy 141 receipts position is set out in the table below. The table sets out the cumulative position to 2015/16 followed by the Council's current projection to 2020/21 (quarter 2).

Date spend needs to occur	Total New Build Expenditure Required (includes 30%RTB)	1-4-1 Receipts
2015-16	4,573,496	1,372,049
2016-17	11,019,592	3,305,877
2017-18	12,039,099	3,611,730
2018-19	12,325,903	3,697,771
2019-20	24,204,721	7,261,416
2020-21 Q2	6,814,384	2,044,315
Total	**70,977,195**	**21,293,158**

The table highlights that the projected total receipts to 2020/21 Q2 are £21.29million, which when grossed up from 30% requires a projected total expenditure of £70.98million.

The current expenditure planned and programmed is set out in the table below, highlighting that £20.96million has been committed to new development expenditure to 2017/18 Q2.

Year	Affordable Housing Expenditure	Cumulative Expenditure
2012-13	2,887,274.35	2,887,274.35
2013-14	737,625.26	3,624,899.61
2014-15	999,308.94	4,624,208.55
2015-16	2,855,761.44	7,479,969.99
2016-17	9,290,995.90	16,770,965.89
2017-18 to Q2	4,190,128.94	20,961,094.83
	20,961,094.83	

The required expenditure to September 2017 (Q2 current financial year) was £21.77million, c£242k more than that committed to date. The Council needs to commit £27.63million by the end of the 2017/18 financial year and plans and programmes are in place to meet this requirement.

The above highlights the scale of the challenge in committing RTB receipts to developments as well as the opportunities for the Council to increase spending on affordable housing development providing schemes can be found which meet the rules set by the Government.