Paradigm Housing Group

VALUE FOR MONEY STATEMENT

2016-17

Introduction

Value for Money (VfM) is integral to how we manage our organisation. Paradigm is a social business, providing low cost housing for those who cannot afford to access a highly priced market. During 2016-17 we continued our focus on providing a fair deal for our residents and using our financial strength to deliver more new homes.

The pressure on families and individuals in our areas of operation is demanding. We operate in West London and the Home Counties to the north and west of the capital where housing costs are high but wages for most workers have not kept pace over the last 5 years. Welfare reform continues to have a significant impact on our customer base in the areas in which we operate, adding to the pressures on household budgets.

New legislation passed in 2016 relating to welfare reform and housing policy will have a substantial impact on our business. Four years of rent reduction is good news for some of our residents but we had to reassess our ability to develop new homes for rent. We implemented plans to reduce costs in 2016-17 and the following three years so that we can continue to deliver new homes. However a greater proportion will be for sale, primarily through low-cost home ownership initiatives.

VfM at Paradigm recognises the importance of delivering quality services efficiently. We benchmark our services against other housing providers and are challenged by our Board to deliver good services at lower cost. Our 2016-17 Business Plan included organisation-wide change projects to help drive value from our assets and deliver cost effective services for our residents through a clearer service offer, better procurement and strong understanding of our asset performance. Our 2017-18 Plan continues the same focus.

As a Registered Provider we are required to meet the requirements of the Regulatory Framework published by the Homes and Communities Agency and these include the publication of a VfM self-assessment. The self-assessment is summarised in our Annual Report and Financial Statements 2016-17 and this document sets out how we are achieving VfM in delivering our strategic vision.

Our strategic aims

Our purpose, reaffirmed by the Board in February 2017, is to make the very best use of our resources so we can provide new affordable homes and a fair deal for existing residents.

During 2016-17, following the 1% rent reduction for social housing lettings, our income per property (excluding property sales but including non-social housing activities) reduced by 0.3% to £6,380. However we reduced related operating costs (excluding property cost of sales) by 10% to £3,260 per property which means we can continue to deliver new homes despite the rent reduction.

Our approach is to use our balance sheet strength to lever in external funding for developing new homes in areas of high demand. In order to continue to strengthen our underlying asset base we must generate profits and the constraints on our future income imposed through changes in legislation mean that we need to continually challenge ourselves to reduce costs. We are committed to offer our existing residents a fair deal, providing good quality and responsive services. In return we expect residents to meet their side of the deal by paying rent on time, behaving responsibly and looking after their home.

We recognise the imperative that we make the best use of our resources, to help those people who need our support. Our strategic targets set out how we plan to achieve this:

Maintaining strong financial health	We will stay financially strong. We know that without a stable financial position we will not be able to help new residents; and we will not put the homes of existing residents at risk.
Running an excellent business	We will run an excellent business, using commercial disciplines, continually striving to deliver efficiency improvements. We will attract high quality staff, invest in their skills and hold them to account for effective delivery.
Making best use of our property assets	We will make the very best use of our existing asset base. We will have a clear asset management strategy and sell or convert stock, as and when we can get better value in doing so.
Investing in new homes	By managing our finances well and driving value in the business, we will be able to invest in new homes. We will continue to offer a range of tenures, including shared ownership and some social and affordable rented housing.
Offer a fair deal to tenants	We will offer a decent service that reflects what tenants want and strikes an appropriate balance in cost terms between the needs of future and existing tenants. We will continue to support vulnerable residents to help them sustain tenancies.
Supporting our customers and investing in communities through the Paradigm Foundation	Our financial strength will enable us to support our customers and invest in local communities, through the Paradigm Foundation. Through this vehicle we will help residents into work, education and training; invest in community projects; and support those facing hardship, working with partners.

Our performance against the strategic targets is set out on pages 5 to 16

For 2016-17, we agreed a programme of key change projects to help deliver the strategic goals. These initiatives cross the whole business as follows:

- **Procurement** – an end to end review of procurement and contract management that will highlight savings targets and quality improvements (page 7)
- **Asset management** – to inform a new asset strategy including strong understanding of return on assets at a granular level (page 8)
- **Tenant deal** – to reaffirm the services we will provide for our residents and what we expect in return; and identifying process improvements to deliver services effectively and efficiently (page 12)
- **Repairs** – to review our Property Services function including cost, productivity and the use of sub-contractors; and how the business commissions and works with Property Services to ensure assurance on compliance and cost-effective, timely repairs delivered to residents
- **Operating model** – to consider the most appropriate model to support our ambitions as an exemplar housing provider, aligning income, cost and service delivery

The 'target operating model' project commenced during 2016-17 and continues through the current financial year with implementation from 1 April 2018. The model places homes and residents front and centre with operations teams having responsibility for delivering services and accountability for profit or loss by housing area. The changes that arise from implementing the new operating model are significant and reach every area of the business including Property Services (as noted above), Development, Asset Management, Finance and IT.

We continue to focus on a number of key indicators, both financial and non-financial, in order to measure VfM in terms of efficiency gains, increased service effectiveness and cost reductions. Further information on these indicators, our benchmarked performance and our targets is set out on pages 14 to 16.

Measuring value for money

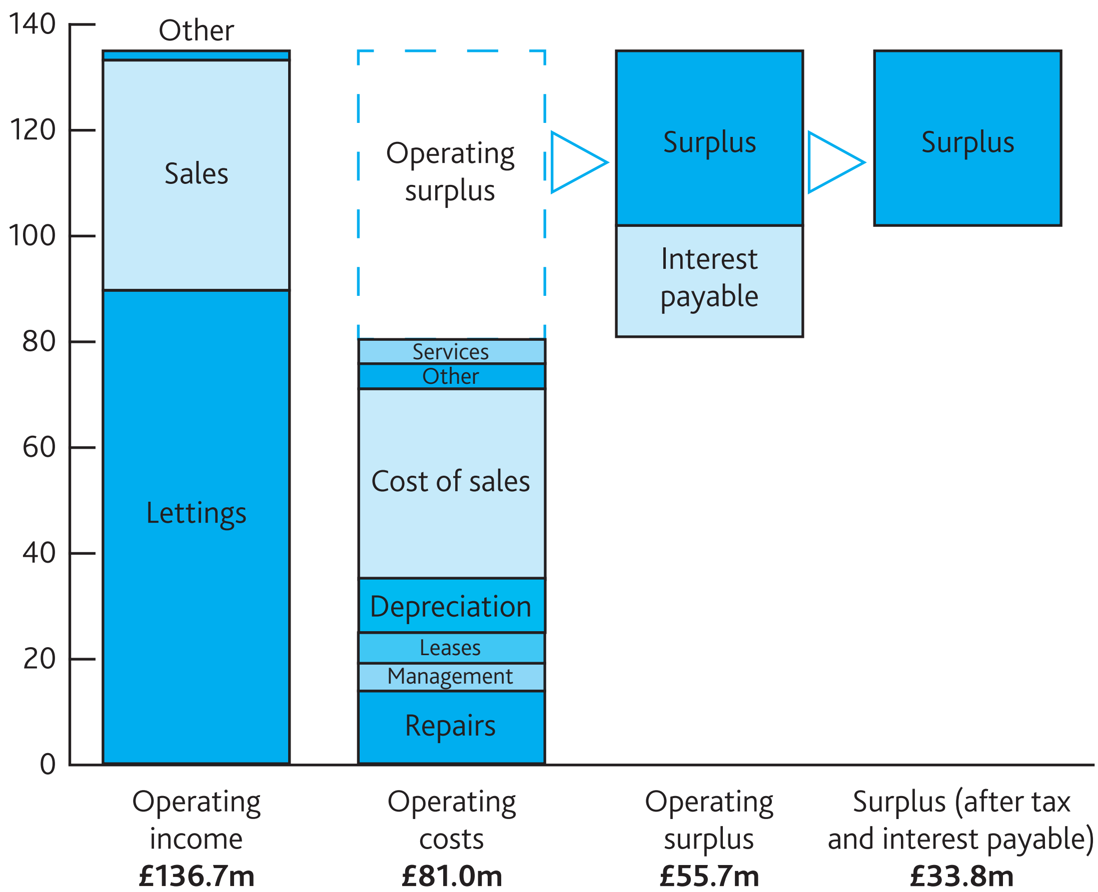
Financial strength

Paradigm's Board is custodian of an important legacy. Our core purpose is to nurture and grow that legacy and protect it and its customers for the long term. This can only be achieved by running a financially sound business. As a charitable housing provider we operate to a clear set of values; however we never apologise for seeking to maximise our profits as every penny is re-invested in new homes or improving services.

Maintaining strong financial health

Our financial strategy has a clear requirement that we should achieve a minimum annual surplus (10% of turnover) and that each part of the business should make a positive contribution to that surplus. For 2016-17 Paradigm Housing Group (the Group) surplus was £33.8m (24.7%), higher in both percentage and money terms than the previous financial year (£21.1m; 18.3%).

Income for the year was £136.7m and a simple breakdown of how we used that money is set out below:



Key financial indicators

					As previously reported (pre FRS 102)	
	2016-17 TARGET	2017	2016	2015	2014	2013
Operating surplus for the year as % of turnover	-	**40.7%**	39.2%	37.6%	32.9%	32.5%
Operating surplus, excluding first tranche surplus, for the year as % of turnover, excluding first tranche/ outright sales	40.0%	**49.0%**	43.5%	42.0%	42.2%	41.6%
Operating surplus from social housing lettings as % of turnover from social housing lettings	-	**50.1%**	46.3%	N/A	N/A	N/A
Annual surplus as % of turnover	10.0%	**24.7%**	18.3%	14.0%	11.1%	11.1%
Rent losses (voids and bad debt as % of rent and service charges receivable)	1.5%	**1.1%**	1.5%	1.6%	1.6%	1.6%
Rent arrears (current tenant arrears as % of rent and service charges receivable)	-	**5.3%**	5.4%	5.4%	5.0%	4.0%
Rent arrears (rolling average adjusted for timing of housing benefit, used for management purposes)	3.0%	**2.7%**	2.9%	2.8%	3.0%	3.7%
Interest cover (Earnings Before Interest Tax Depreciation and Amortisation divided by interest payable and capitalised interest)	1.4	**2.0**	1.8	1.6	1.6	1.8
Interest cover (Earnings Before Interest Tax Depreciation and Amortisation, Major Repairs Included, divided by interest payable and capitalised interest)	-	**1.9**	1.4	N/A	N/A	N/A
Gearing (total loans less cash as % of capital employed)	<70.0%	**56.4%**	57.5%	57.3%	55.5%	63.8%
Return on investment (earnings for the year as % of average total debt)	7.0%	**7.6%**	7.5%	6.6%	6.5%	5.9%
Return on assets (surplus for the year as % of average total assets, adjusted for property revaluation)	1.8%	**2.5%**	1.7%	1.3%	1.7%	1.6%

In order to develop and grow our business our aim has been to generate at least 40% operating surplus (excluding the impact of sales) so that we build net worth, enabling us to borrow and invest in new homes. As noted last year, our focus is to at least maintain operating surpluses, in spite of the government-imposed reductions in rental income. We are pleased to report an operating surplus of 49.0%, excluding sales, strengthening our interest cover and reflecting efforts across the business to bear down on cost.

The interest cover indicators show the level of headroom on meeting interest payments for current levels of debt and both indicators have increased since last year-end. EBITDA-MRI, calculated to take account of capitalised repairs increased to 190% (2016: 141%).

In maximising our borrowings a key restriction is the availability of security for new loans. Increasing numbers of new properties are shared ownership and on larger developments, built out over longer timescales than traditional schemes. In future we anticipate more of our developments are likely to be for sale, primarily on a shared-ownership basis. Effective treasury management continues to be critical for developing social landlords like Paradigm.

Treasury

As a business we borrow a large amount of money to fund the development of new homes. Our total borrowings at 31 March 2017 were £751.0m, a slight increase in borrowing per property to £55,067 (2016: £52,458). The increase was expected following the Board decision to mitigate risks associated with market uncertainty by ensuring funds drawn down well in advance of requirement, a 'buffer' of £30m plus two-years' planned development spend.

We remain dependent on borrowings and a robust treasury management strategy is essential. Key treasury facts and achievements during 2016-17 include:

- Average cost of fixed rate funds is 4.9%
- Over 39% of debt fixed for more than 20 years
- Six months of cash secured and available at any time

We are considering potential opportunities to drive down the cost of funds and increase headroom.

Procurement

Effective procurement, which supports business objectives, will deliver financial and qualitative benefits for us and our customers. During 2016-17 a review of procurement processes, including on-going contract management, commenced as one of five key strategic projects that will help deliver VfM across the business. The first stage concluded in 2016-17 with recommendations including strengthening the procurement team to support delivery by the business of identified savings exceeding £1m per year, with £750k in the first year (2017-18).

We have already embedded measures which will deliver £1m of recurrent annual savings, with key areas relating to insurance and our commercial vehicle fleet. In last year's VfM report we identified areas for review during 2016-17, together with indicative new procurement savings, as follows:

Area of business	Procurement savings £'000	Comment
Property services	800	Materials; van stock. Further savings anticipated from improved contract management and better utilisation
Central costs	140	Legal services; printing, postage, stationery
Estates	300	Service and utility costs
	1,240	

Our financial performance for 2016-17 reflects the savings identified. Within property services in particular significant savings have arisen from substantial reduction in using sub-contractors and we anticipate further efficiencies from improved contract management and better utilisation.

Service charges and costs

Our service charge policy is to recover costs in full from those residents who benefit from the services. However VfM is not only about recovering costs but also about minimising those costs wherever possible against agreed service standards. Savings arising from scrutinising and challenging utility bills continue to be identified and are passed on to residents in lower annual charges. Where the challenge results in repayment of personal heating charges, of between £1 and £600 per person, these are refunded directly.

Making best use of our property assets

Any business wishing to achieve financial efficiency will optimise the management of its assets and Paradigm is no different. Changes to the way in which major works are planned, together with targeted disposals, will improve the quality of the stock, the outcomes for customers and generate significant resources for investment in new homes.

Our main portfolio is social housing assets and we achieved an overall operating surplus, excluding build for sale, of £44.5m in 2016-17, equivalent to an operating margin of 49.0% which is far in excess of the 27.3% average achieved by the registered provider sector according to the HCA's 2016 Global Accounts. Our operating margin from social housing letting activities alone has strengthened to 50.1% (2016: 46.3%).

Our asset management strategy, setting out our approach to ensure that our assets meet our longer term requirements in terms of location, condition, cost in use and rate of return on investment, is under review. Our focus has been to optimise asset location, in four different strategic ways to reduce operating costs:

Acquisition	We acquire housing stock from other housing providers where the location means that we can increase the density of our property base in different geographic areas and achieve economies of scale.
Development	A key part of our evaluation of a new scheme is whether it is adjacent or near to existing Paradigm properties to 'infill' our footprint and minimise operating costs.
Disposal	We review which properties we should dispose of as they become vacant. Our approach has been reactive, considering individual properties rather than identifying in advance those assets that we may wish to dispose of due to condition or value.
Rationalisation	Where we own and manage properties outside our core operating areas, making the properties more expensive to manage and maintain as well as meaning residents may experience a lesser service, we have sought to dispose of the properties to other registered providers. The last time we undertook a significant rationalisation disposal was 2013.

We do not anticipate a radical change but rather to refine the approach taken so that pro-active decisions are based on the latest information on stock condition and value.

Our in-house IT system reflects strong integration between the finance, development and investment works systems so that we have up to date information on the age and cost of the key components in our properties. We are undertaking a full stock condition survey to confirm that the information held on the system is accurate. The survey has been in progress for over a year and is expected to complete in 2018.

In the meantime we use the asset information as part of our review of void properties to determine their best use – for refurbishment and re-letting or disposal; for example some properties which have poor sound insulation require significant investment to bring them up to standard. In 2016-17 we generated £1.7m from 13 empty property sales.

For those properties that we keep and re-let, the conversion to Affordable Rents (AR) increases the future rental stream and allows us increased borrowing ability as a consequence. In 2016-17 we converted 182 properties, increasing income by £560k, enabling additional borrowing of £13m.

We maximise our operating surpluses by ensuring that our properties are of good quality and in demand, keeping voids, bad debts and arrears low, and driving down costs of management and maintenance. Following our review of voids and lettings reported in last year's VfM Statement, we have implemented the recommended structures and management arrangements. A reduction in void times from 22 days to 13 days in 2016-17 (just short of the 12 day target) resulted in a reduction in void rent losses in the year of over £200k. In 2017-18 we are continuing to focus on lowering void costs through minimising both days to let and overall void costs (including repairs).

One of the key projects that began during 2016-17 as part of our change programme is a review of asset management. Expected outcomes include recommendations for system changes to support a new asset management strategy, due in October 2017, to ensure our assets meet our longer term requirements and to move away from the current reactive approach to investment/disposal decisions when properties are becoming void. We anticipate a more granular approach to return on investment so that we have a clear view of the rate of return on individual assets.

Investing in new homes

Our core social purpose is to provide new affordable homes for people who cannot afford to rent or buy in the open market. We aim to provide a range of housing solutions and see the implementation of a prudent and limited outright sale programme as a way of subsidising our affordable homes programme. However we need to manage our exposure to sales risk and one way that has proved effective has been to shift between tenures, particularly from outright sale to shared ownership where we have been able to access appropriate grant subsidy.

Our development activity is funded from three principal sources: proceeds of property sale; capital grant; and borrowing. Reducing levels of grant and rental income mean we have had to take action to reduce our revenue costs (housing management and maintenance) as well as maintain our surpluses from sales in order to continue to invest in delivering homes for future customers.

Development appraisals for rented and low-cost home ownership properties reflect the total cost in use for residents, to ensure they receive value for money in the enjoyment of their home. Each scheme proposed for Board approval highlights the estimated weekly outgoings for each property type including rent, estimated utility bills, council tax and service charges.

In appraising new schemes we target return on investment (ROI):

Activity	ROI target
General social housing	**5.0%**
New business opportunities and development	**7.0%**
Commercial activities	**10.0%**

We currently achieve 7.6% overall, measured as operating surplus (excluding build for sale) divided by external debt.

Highlights of our development and sales activity during 2016-17 include:

- 403 homes completed for rent or sale, including shared ownership
- 1,634 homes started and under development at the year-end
- Sold 236 new homes under market sale or shared ownership generating £46.0m income and £11.2m profit
- Delivered our HCA and GLA commitments
- Entered into dialogue with Chiltern District Council to discuss how we might maximise use of brownfield sites to support delivery of their Local Plan.

Supporting our customers and investing in communities through the Paradigm Foundation

We established the Paradigm Foundation in 2013 with a donation of 2% of annual profits. Having the Foundation enables us to 'ring fence' our added value and social value work so that we can focus on the core business of providing homes and housing services that our customers value. The Foundation is led by a board of trustees and operates independently from Paradigm, although we remain its largest donor.

Key aims are:

- Supporting residents and their families into work, education and training
- Alleviating financial hardship through initiatives and small grants relating to income maximisation and financial welfare
- Encouraging community involvement through grant funding for small and larger community projects.

Achievements during 2016-17 included:

- £70k grants awarded to Citizens Advice Bureaux (CABs) across the areas in which Paradigm operates, to enable their work providing debt advice, counselling and support, with a further £50k per year awarded last year but allocated for two years to support the Bucks Money Advice Service (BMAS), established through joint working with Chiltern, Wycombe and Aylesbury CABs. The service launched formally in June 2016 and has received publicity through the local press and via the CABs; and a review of their achievements in 2016-17 highlighted 847 Paradigm residents had been supported during the year. We plan to work with other CABs and registered providers to promote similar joint approaches across other geographical areas so that even more people can benefit; starting with Welwyn-Hatfield CAB in Hertfordshire
- £120k grants provided to a number of other not-for-profit organisations and community groups across the areas in which Paradigm operates to underpin wide-ranging projects including: The Oasis Partnership, supporting people with dependency on drug and alcohol; Home Start, supporting families; ToolShed, offering further education, training and business skills for young people in more deprived areas; and local youth clubs
- 18 small individual grants allocated to Paradigm residents for education and training, including work-based schemes to help them into employment, and relief of financial hardship.

We have agreed with the Foundation to undertake a review of the social and economic impact of their work to inform future investment decisions but due to competing priorities the study anticipated to be commissioned in 2016-17 has been deferred to later this financial year.

Customer satisfaction

Our customers want us to deliver to agreed standards as reliably and efficiently as possible. As one of the corporate change projects we have continued to develop the 'deal' with our tenants, so that we are clear about what we commit to do for our residents and about what we expect from them in return. The first stage is complete and sets out a clear statement of repairs responsibilities between Paradigm and tenants; updated investment works standards (kitchen and bathroom replacements); and a new void repairs standard. The next stage is implementation of the deal and new performance measures and targets during 2017-18 and we will report further on the outcomes in next year's VfM Statement.

Running an excellent business

In order to deliver a service with minimum waste it is important to provide clarity for both customers and staff about what we can and can't do. Our customers have told us what is important to them and our service standards focus on keeping customers informed; personalising responses and tailoring services; resolution of issues; and reliability and responsiveness.

We recognise that the success of our business depends on the quality of our managers and staff and our performance against key targets is summarised below.

Key targets	Outcomes
To use our business and customer intelligence on impact, cost and affordability to drive improved standards	**Achieved** – we spoke with a number of customers as part of the tenant deal regarding the service they receive and what matters to them most. Their responses helped inform a suite of indicators developed to drive performance improvements and inform operational decisions that are being reported monthly to Management Team.
Greater accessibility and self-service options	**Achieved** – plans for 2016-17 included updates to the corporate website and customer portal which have been implemented, although slightly later than planned, in August/September 2017.
Produce easy to read and accessible standards for customers and staff	**On-going** – reviewed and updated as part of the tenant deal; and repairs standard implemented from April 2017.
To have a comprehensive training strategy from induction to leadership development	**On-going** – the introduction of the Apprenticeship Levy has broadened our use of apprenticeships from Property Services across the wider business. A new talent management process will be implemented during 2017-18.
To introduce a new Total Reward strategy	**On-going** – a new Head of HR has recently been appointed and is leading a Total Reward project that is planned to complete by the end of the current financial year (2017-18).
To introduce and embed the new governance structure and to carry out a thorough governance compliance assessment	**Achieved** – recommendations from the independent review of the governance structure to ensure it aligns with our plans for delivering future services have been implemented in full.

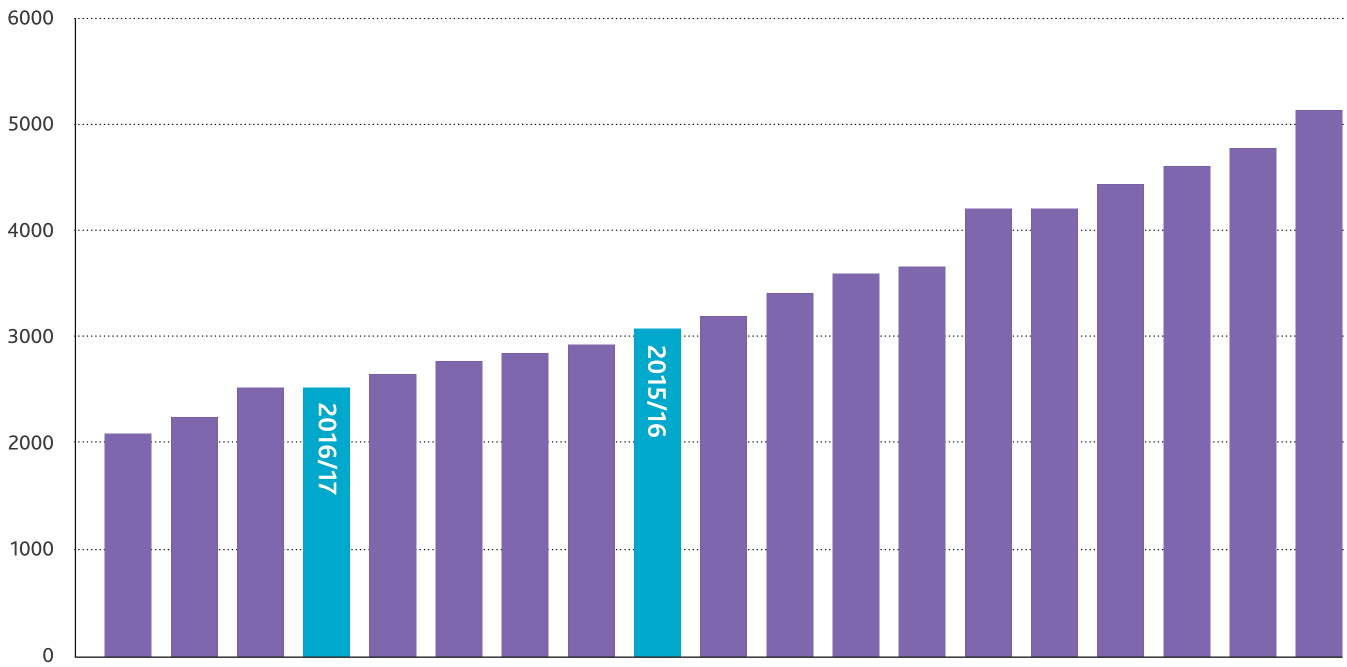
Benchmarking and Performance

Our operating surplus is high by comparison to our peers and in 2016-17 we reduced overall cost per property (including capitalised major repairs) by 13% to £3,636 (£3,260 excluding capitalised major repairs). We will continue to bear down on costs during 2017-18 so that we continue to generate healthy surpluses in spite of the challenge of lower rental income through government-imposed rent reductions.

Most sector-wide benchmarking information relates to social housing performance. The HCA has provided comparative information for social housing for 2015-16 and our headline social housing cost per unit was £3,453, lower than national average (£3,960) and median (£3,550).

Refining the comparator group to include only Registered Providers in London, South East and East of England with between 7,500 and 15,000 social housing properties (and excluding service costs which distort the comparison where providers have supported housing) our total social housing cost per unit was £3,149, below group average (£3,451) and median (£3,250). The total cost per unit reduced further for 2016-17 to £2,554, exceeding our target to reduce costs by 10%:

Figure 5 Benchmarking performance against 17 other Registered Providers in London, South East and East of England – Total Cost per unit 2015-16



Source: HCA Global Accounts 2016 Unit Cost Data

We are participating in the Sector Scorecard pilot testing alternative benchmarking solutions that are expected to include more financial indicators for 2016-17 and subsequent years.

Following the review of key performance indicators early in the financial year, we introduced a 'balanced scorecard' covering both financial and non-financial indicators for the whole business. The indicators are reviewed monthly by management and quarterly at Board meetings. At the year-end the overall results were generally strong reflecting significant improvements over the previous year for key areas of focus:

- financial strength
- rent arrears
- voids and lettings
- repairs and maintenance
- customers

An extract from our balanced scorecard (below) shows very strong operating performance although the number of homes completed in the year fell below target, with two schemes completing shortly after the year-end to bring this back in line. The average sales margin per property was adversely affected by a lower margin for one scheme where the sale was at an agreed lower price to a local authority, although still generating a surplus for the business.

Last year we reported a reduction in re-let times from 26.2 days in 2014-15 to 22.1 days. For 2016-17 our target was a challenging 12 days. Following a major review of voids and lettings that started in 2015-16 and concluded in 2016-17 the average re-let time for the year reduced to 13.2 days, not quite achieving target but a significant reduction from the prior year which was a key contributing factor lowering the void rent loss by over £200k.

There are a number of areas where efforts continue to bring performance in line with target for 2017-18, in particular completion rates for emergency repairs and 'first time fix'.

PERFORMANCE INDICATOR NAME	2014-15	2015-16	Target 2016-17	2016-17	Target 2017-18
Financial					
Interest cover (EBITDA)	1.6	1.8	1.4	**2.0**	1.4
Operating margin excluding first tranche sales	42.0	43.5	>40%	**49.0**	>40%
Gearing Ratio	57.3	57.3	<70%	**56.4**	<70%
Arrears as % of Turnover (4 week average, all properties)	2.86	2.94	3	**2.72**	2.8
Operational					
Number of homes completed	444	542	500	**403**	600
Average sales margin per property (%)	N/C	28	>15/16	**26**	28
Average standard re-let time (days)	26.2	22.1	12	**13.2**	12
% repairs completed within target time - Emergency	96.5	99.2	99	**97.9**	99
% repairs completed within target time - Routine	86.0	89.1	90	**93.5**	90
% of repairs categorised as 'right first time'	85.4	88.9	90	**87.2**	90
Cost of reactive and cyclical repairs per property (£)	N/C	1,384	<15/16	**1,220**	<16/17
Cost of improvement works per property (£)	N/C	888	<15/16	**637**	<16/17
Customer					
Average Customer Services call rate per property	N/C	11.0	<15/16	**9.8**	<16/17
% chase calls in the repairs CS team (per month)	N/C	17.2	<15/16	**14.0**	<16/17
Average number of days to resolve all complaints	20.4	10.7	15	**13.8**	15

Note: Cost of voids (whole cost measure of rent loss and void works) to be introduced in 2017-18
N/C: not computed for 2014-15 (not previously used as indicator)

Conclusion

Paradigm's Value for Money Statement has been designed to demonstrate our holistic approach to achieving value for money. We do not see this as a 'one-off' statement but rather report of our successes in the past year and on-going improvement plans designed to strengthen the effectiveness of our services whilst controlling and in some circumstances reducing costs.

Our overall commitment to value for money is referenced in a number of corporate documents (rather than restricted to this Statement) including: Business Plan; Annual Report and Financial Statements; and Annual Report to Residents, highlighting the different ways we embrace VfM.

We have not yet achieved all our targets and the Board and Executive are focussed on meeting the targets set out in this statement. In some instances we have achieved and are exceeding the objectives and have set more challenging targets going forward (for example rent arrears). We will continue to take this approach in future.