Housing Revenue Account
Business Plan and Capacity Summary

FINAL

Report v1
2 January 2024

Contents

1. Introduction

The London Borough of Ealing (LBE, the Council) have appointed Savills to support officers in the production of the annual Housing Revenue Account (HRA) Business Plan model.

This builds upon the work that officers have undertaken in previous years in establishing a fully refreshed HRA Business Plan. However, to add value, LBE have now adopted the Savills HRA Business Plan platform for ease of operation and scenario testing. LBE, like many authorities, need to adopt a new approach to setting out the financial capacity and capability of the HRA to deliver on its objectives towards refurbishment, investment, regeneration and new supply. Consideration of a new approach is also consistent with the requirement for the publication of Prudential Indicators specific to the HRA following their reintroduction alongside the abolition of the debt cap.

2. Business plan model

2.1. Introduction

Our latest version of the HRA Business Plan model has been provided and populated in liaison with officers in order to progress the 2024.25 budget process and forms the basis of this report. It will continue to have revisits in respect of updates to the asset management strategy and any forthcoming estate regeneration amendments as further details become available from those included within this plan.

2.2. Overview of methodology and assumptions

Overall

The plan is based on the following overarching principles:

- Balanced to the 2023.24 latest projections for the HRA
- 29 year projections from 2024.25 based on the provisional 2024.25 budget
- Core inflation projected at 2.0% thereafter with exceptions as detailed below
    - 2.5% for April 2025
- Rents increasing at CPI per annum with the exception of the following:
    - 7.7% April 2024 (on the basis of the current final year of the social housing rent policy, applying September 2023 CPI +1%), 2 Years thereafter at CPI +1% (assumption that the current policy will be extended for 2 years)
- Service charges increase in line with rents with the exception of 2025.26 where an additional 10% is modelled as provisional increase on the potential outcome of a forthcoming service charge review.
- Depreciation adjusted for 2024.25 based on a revised basis for calculation (subject to audit approval).

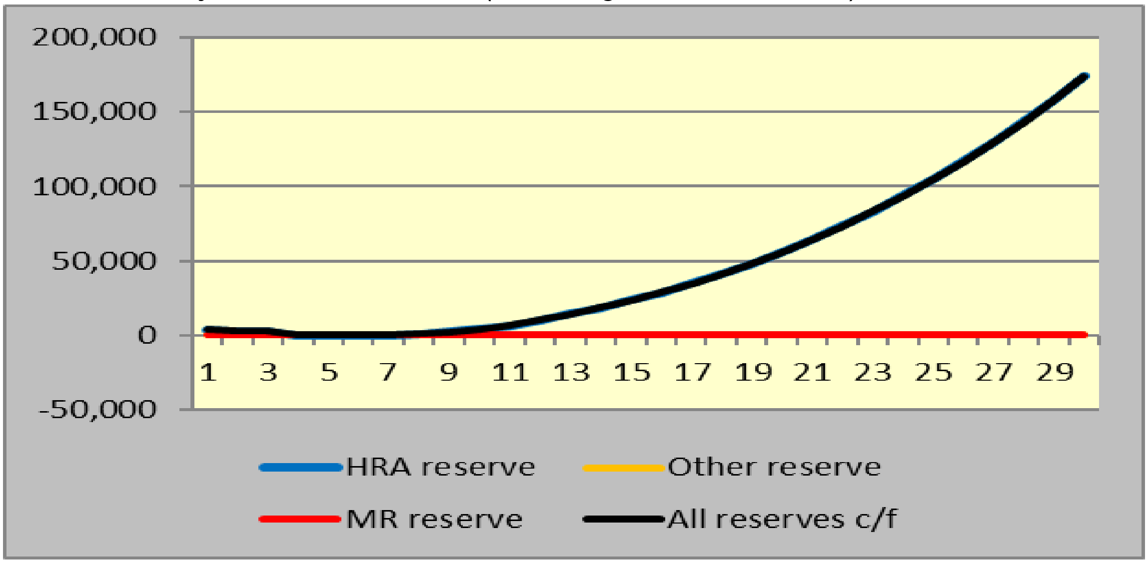
- Due to a revaluation of the repairs budget and the impact of inflation, damp and mould and disrepair claims the forecast expenditure for 2024.25 increases by £2.8 million, some 13.5% from the revised 2023.24 forecast of £20.836million. The original 2023.24 budget was originally agreed at £15.107million, with the reported forecast a growth of £5.729 million or 37.9%. Proposed reductions of 30% have been modelled in 2026.27 to bring repairs costs down to similar levels to the original budgets for 2023.24.
- Management Costs increase in line with CPI although a 5% reduction in overall costs is modelled in 2025.26 in anticipation of a review of the cost of services and potential efficiencies.
- Maintenance of the existing tenanted stock (subject to Right to Buy sales and excluding estate regeneration) is modelled at a total of £722.4million over the 30 years from 2023.24
- Provision of £316.2million for the estate regeneration and new build programmes (with subsidy contributions of c£95.4million) delivery a net loss of 14 properties.
- The inclusion of 64 loans directly attributable to the HRA, that are at fixed interest rates for varying periods.

The overall methodology within the plan is also founded on net rental income servicing the operational expenditure, interest charges, and where required, additional borrowing to finance investment to the stock and loan refinancing when existing loan facilities mature.

2.3. HRA Business Plan projections

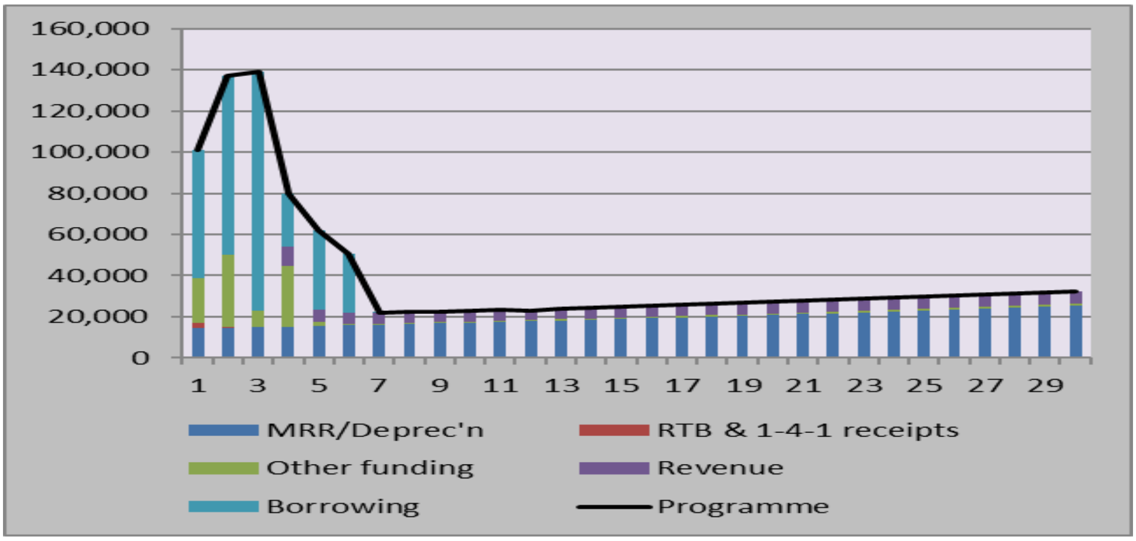
As a starting position for financial forecasting an agreed set of assumptions relating to inflation and interest rates are factored in. LBE currently hold £4.925million in a separate reserve, which in effect is for unforeseen contingencies. Therefore, this reserve is excluded from the projections below.

Chart 2.1 – Projected HRA balances (excluding minimum reserve)



Without including the minimum reserve balance of £4.925million the above graph demonstrates that from year 4 the HRA produces sufficient surpluses to contribute towards capital expenditure. From year 9 balances begin to accrue to c£174million by year 30.

Chart 2.2 – Projected capital expenditure and financing



Capital expenditure is fully funded throughout the 30 years, demonstrated by the horizontal black line. There is a significant increase in projected expenditure in the early years to meet the requirements of building safety works and energy efficiency improvements plus additional provisions in addition to the new build and regeneration programme. In order to part finance this, additional borrowing is required, which in turn results in additional interest charges which has a negative impact on HRA reserve balances. Inflation has been included within the above projections, with the exception of years 3 to 6.

Chart 2.3 – Projected Capital Expenditure (By Category)

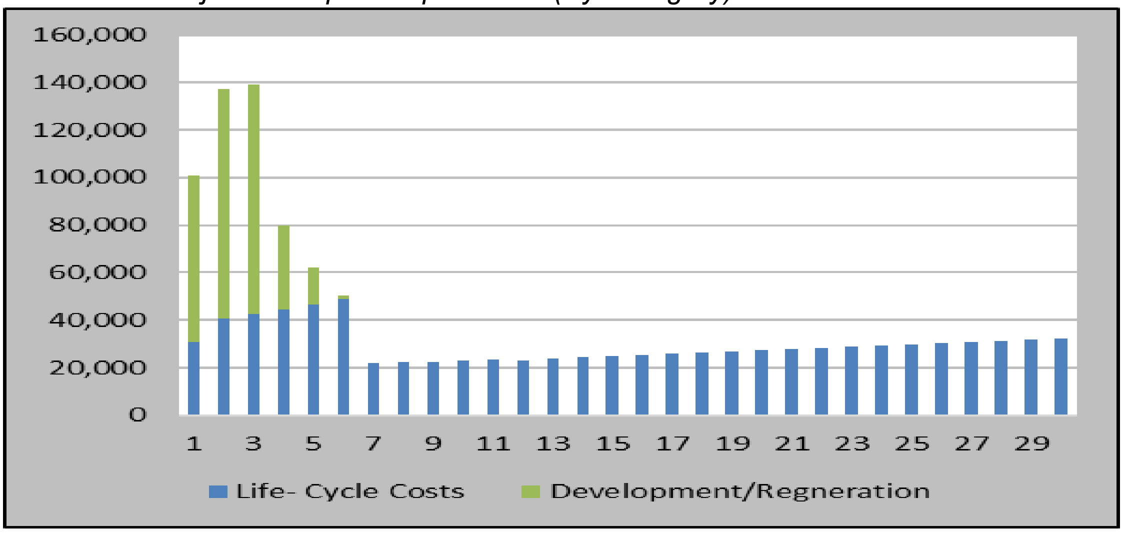
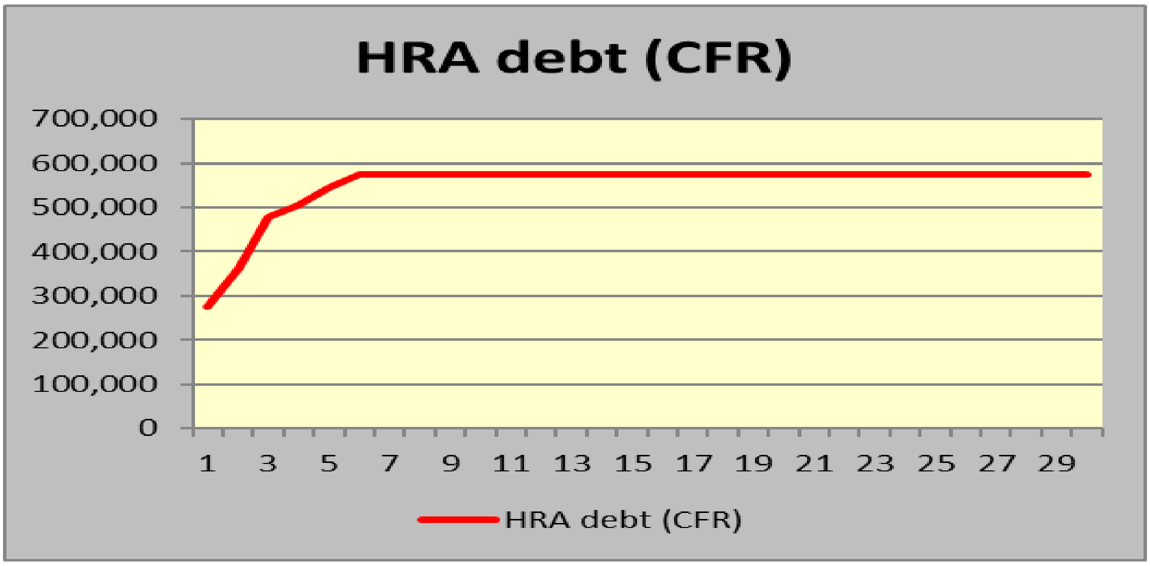


Chart 2.4 – Projected debt profile (HRACFR)



Borrowing is projected to initially peaks in year 6 at £572.9million from an opening position of £213.9million and remains at this level throughout the remainder of the plan. All of the existing loan facilities that mature during the period of the plan are refinanced as demonstrated in the chart below.

2.4. Debt in Comparison to Provisional Prudential Limits

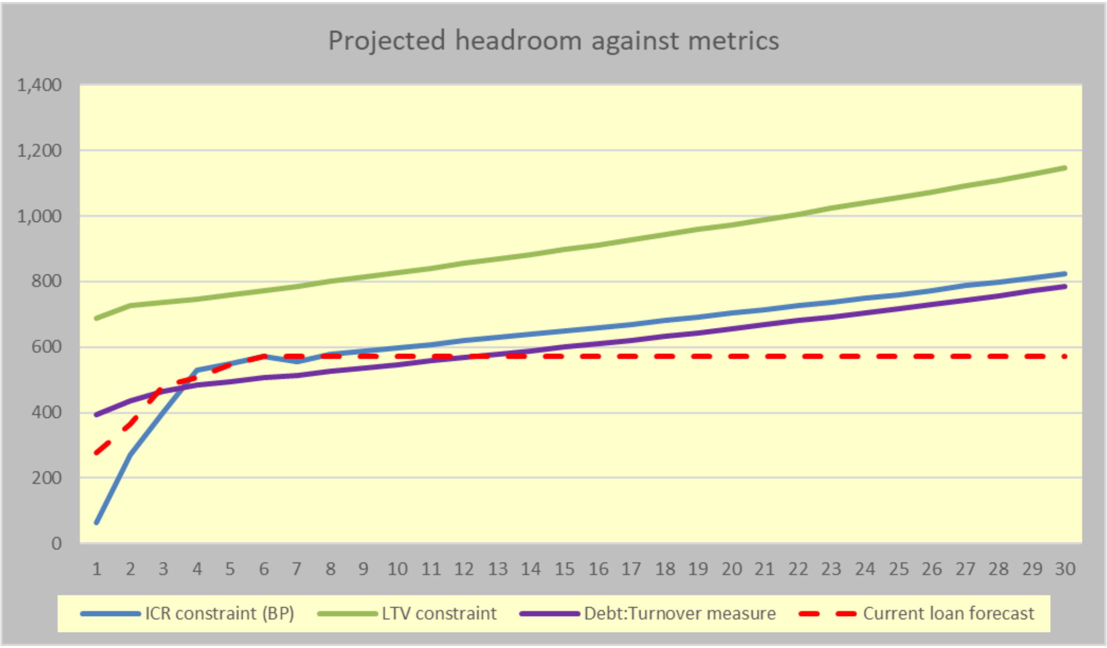
The HRA debt cap represented an artificial constraint on borrowing set outside the HRA and linked to future income and cost assumptions which were made in 2012. The housing and financial policy environment has moved on considerably since then, however the only change in the debt cap implemented was for a small minority of authorities that opted to bid for an increase in 2014.15.

Whilst there is theoretically now no limit to borrowing within the HRA, the existing asset and operating base generates a net income stream that does offer a logical limit on sustainable borrowing levels. In setting out its investment strategy, the Council therefore needs to consider how it will take decisions on whether to invest, how to fund, the extent of new borrowing, and determine a framework within which decisions will be taken for the business plan overall, within the medium term financial strategy and within successive budget rounds.

This report applies some metrics developed in the light of the experience of 40 years' of successful private finance of housing associations, during which associations have developed hundreds of thousands of new affordable homes, without a single association ever going into default with any of its lenders.

This is not the only approach that can be utilised, for example the Council will have an established approach to the setting of Prudential Indicators in the General Fund which it might wish to consider in the HRA context. However, as will be seen, looking at tried and tested principles from a privately financed sector in the HRA context provides a powerful and persuasive evidence base for a significant increase in funding for new HRA developments.

Chart 2.6 – Projected Debt (HRACFR) Compared to Provisional Borrowing Limit



The red (dashed) line shows the projected loan balances, as per chart 2.4 set against the three "golden-rule" suggested metrics.

Using the Loan to Value metric of a maximum of 65%, the plan suggests that there is scope for borrowing headroom which is measured by the gap between the green and red (dashed) line.

The Debt to Turnover ratio, maximum of 5:0, suggests that borrowing will exceeds the "golden-rule" modelled from year 3 to year 12 of the plan.

By default, the Interest Cover Ratio is considered the benchmark for assessing borrowing capacity and using the "golden-rule" of a minimum of 1.25, the projected borrowing remains broadly above this level until year 7 of the plan.

3. Sensitivity Modelling

We have modelled a range of scenarios that demonstrate the impact to the plan, which can be considered more externally influenced, as per the table below.

Table 3.1 -Sensitivity Table

Sensitivity £'m	HRA Bal Yr 30	Debt Yr 30	Minimum Headroom ICR From Year 4 (Year)	Borrowing Limit at Year 30
BASE	**174**	**573**	**-16 (7)**	**823**
Inflation +0.5% pa	266	571	-1 (7)	943
Inflation -0.5% pa	90	576	-32 (7)	719
Interest -0.25% pa	203	570	5 (7)	859
Rents CPI +1% all years	692	570	24 (4)	1,604
Rent Freeze (Yr 2 – 2025.26)	55	600	-87 (7)	735
Capital Expenditure +5%	122	588	-28 (7)	824
Capital Expenditure Inf +1% 5 Years	131	579	-21 (7)	824
Repairs Expenditure Infl +1% 5 Years	139	576	-36 (7)	797
If Repairs Savings Halved (15%)	32	611	-104 (7)	712
If No Management Savings Achieved	90	588	-64 (7)	761
Right to Buys (Reduced by 50%)	222	572	-5 (7)	909
Voids +0.5% Bad Debts +1%	134	578	-39 (7)	795

The plan shows a varied impact to both positive and negative sensitivities. Areas of concern will more in respect of reserve balances and residual debt that the HRA has at year 30, although there is no statutory requirement for repayment, and the reduction in borrowing headroom. A further consideration is the adoption of prudential borrowing rules. The table excludes year 1 to 3 for the ICR analysis on account of the period prior to proposed and assumed efficiency savings modelled.

4. Summary

The HRA business plan forecast as set out in our modelling for the London Borough of Ealing shows the current projected financial position and future potential borrowing capacity. By borrowing immediately, the plan demonstrates that debt goes beyond some of the provisional golden rule levels set within the plan, particularly in the early years. The plan does require substantial borrowing in order to finance the identified capital investment, which the arising interest charges can met but only due to the revenue efficiency savings modelled.

This report should provide a basis for the Council to inform its future approach to establishing a decision making framework for its HRA investment and development strategies, and also inform the work to be undertaken to adopt Prudential Indicators for the HRA.

Appendix 1 Key Assumptions

	Assumption	Notes
Dwelling Rent	7.7% Increase 2024.25 then CPI+1% for two years then CPI only thereafter	
Void rates	3.27%	

Service Charges	CPI +1% for 2 years then CPI only 10% increase assumed in 2025.26	Full service charge review to be carried out
Non dwelling (commercial) rents	CPI only increases after adjustments to base budget	
Garage Rents	CPI only increases after adjustments to base budget	
Major Works Leaseholder Contributions	Linked to Capital Programme	
Repairs and Maintenance Costs	CPI only increases 30% reduction modelled in 2026.27	
Management Costs	CPI only increases 5% reduction modelled in 2025.26	
Heating and hot water charges	CPI only increases	
Interest rate on borrowings	Based on Existing actual rates c3.28% then long-term average of 3.5%	
Depreciation	Straight Line Basis over life of Assets	

Appendix 2 Benchmarks

Outer-London Benchmarks for Financial Year 2021.22 (noting that 2022.23 accounts are still in the process of being published by boroughs).

Metric	**Ealing 2021.22**	**Outer London 2021.22 Average**	**Ealing Forecast 2023.24**
Rented Properties	11,773	9,252	9,909
Gross Management per unit	£2,650	£2,682	£4,111

Net Management (less service charges) per unit	£2,030	£1,908	£2,543
Repairs per unit	£963	£1,191	£2,102
Gross Management and Repairs per unit	£3,613	£3,873	£6,213
Depreciation per unit	£1,344	£1,241	£1,486
Average Rent (52 week basis)	£100.12	£110.53	£108.34
Other (non-Service Charge) Income per unit	£213	£179	£133
Operating Surplus per unit	£511	£1,273	£173
Operating Margin	9.3%	19.5%	2.18%
Debt per unit	£15,956	£20,465	£26,013
Interest per unit	£604	£539	£972
Interest Rate	3.79%	4.01%	4.09%
Reserves per unit	£418	£1,619	£915