Value for Money

self assessment **2015/16**

Catalyst

Value for Money

Introduction

At Catalyst our purpose is 'To use our wealth, assets and talent to provide housing solutions and opportunities for those who cannot afford a home without our help'. We aim to put VfM at the heart of everything we do. During a year that has brought new challenges to the housing sector we have redefined our corporate vision and set new goals for the business to achieve by 2020. Our vision is:

"To create a self-sustaining business, which uses commercial disciplines and profits to provide affordable homes, improve neighbourhoods and change lives".

We have identified that we need to improve in some areas to deliver real value for money from our services. In particular, we are transforming service provision to harness efficiencies from technology, and focussing asset management activities to maintain high standards while reducing total spend. In short, we aim to do more with less, and are relentlessly working towards improving our margins and increasing our surpluses to re-invest in building new homes. We are working to create an operating model that is efficient and generates positive outcomes for our customers while remaining resilient to emerging risks and agile enough to seize opportunities.

We define value for money as 'using our resources to deliver more of what our customers value'. That means spending our money wisely, using our corporate health to drive value through our supply chains, attracting great people to work for us and driving them to perform at the highest level. We are developing new housing solutions to meet the diverse needs of our current and future customers, and modernising service delivery in all areas of the business. The socio-economic changes and challenges in our operating area give us motivation to find better ways to meet the needs of our customers.

We have responded positively to the significant changes in our operating environment during 2015/16, and are continuing to develop our VfM strategy. Our VfM objectives during the year have focussed on three key areas:

- **Making best use of our assets and creating a dynamic asset management strategy**

We have completed the implementation of our new asset management system which provides visibility at a granular level of our asset data, and has significantly improved our ability to accurately forecast future improvement and planned maintenance works. In addition, we have assessed all our rented properties via our asset grading model. As a result, we have begun a series of options appraisals and are planning a self-funding programme combining selective disposals with improvement works.

- **Improving our operating margin by achieving significant savings in operating costs**

Our financial results for the year to March 2016 were our best ever. We have reduced our operating costs, achieving an operating margin on social lettings of 32.9% compared to 30.1% in 2014/15 and beating our target of 30%. We are not resting on our laurels: we have set a challenging budget for 2016/17 that seeks to continue this trend, whilst absorbing decreases in rents and undertaking a pan-organisational transformation programme.

- **Continuing to deliver better services for customers and increasing social return**

Whilst many of our service performance indicators recorded improvements, we recorded a fall in overall satisfaction among our customers for the second successive year. Our triage model for customer interventions continues to deliver excellent results, and we have achieved a great deal through our sustainability strategy. There is information on the work we are doing to improve customer satisfaction later in this report. In the immediate future we are looking to transform our approach to customer service, and have a target to shift 80% of service delivery to digital platforms by 2020. We will continue to respond to more complex issues via our newly created Neighbourhood Experience Management teams, ensuring scarce resources are focussed where they are most needed.

Our goals for 2020 include leveraging best use of our assets and becoming a top quartile performer for operating margin and profitability. We have undertaken a transformation programme to reposition the business, and transform the culture to promote high performance and innovation where we:

- Are creative
- Do more with less
- Don't tolerate waste
- Drive out mediocrity
- Live our Making It Easy culture
- Recruit people who will deliver the future
- Have a clear deal with our customers.

The key ingredients of our transformation programme include further reductions in our operating costs, implementing a digital strategy, and a new integrated approach to asset management. This VfM Report contains details of the work we have already completed to deliver enhanced VfM, along with the challenges we have set ourselves for the immediate future.

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Financial outcomes

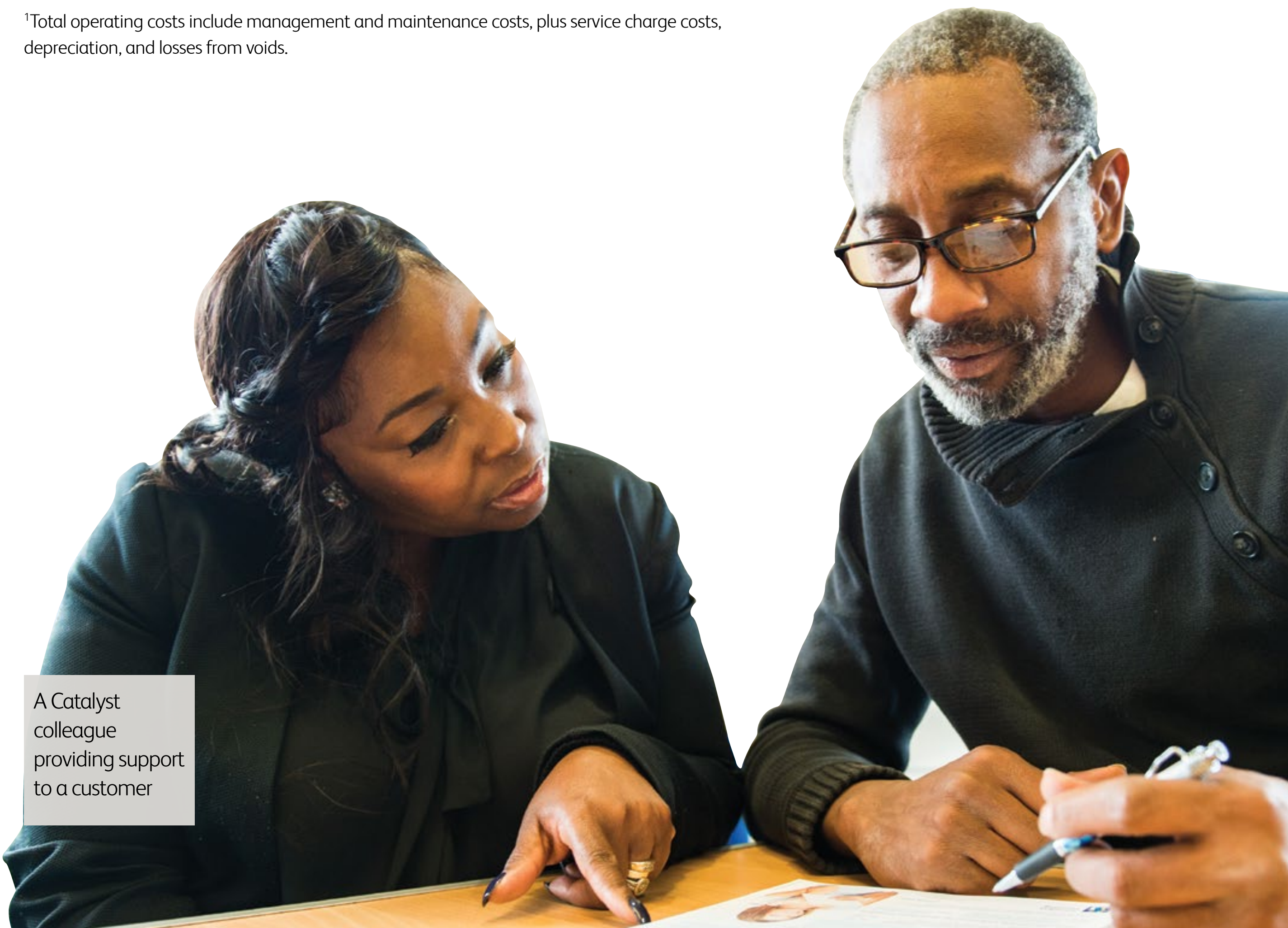
As financial pressures have continued to impact our business we have continued to target reductions in our operating costs and to raise our margin above 30%. Our March 2016 Financial Statements confirm an operating margin on social housing lettings for the year of 32.9%, and a net surplus before tax of £72.9 million. These are both record results for Catalyst.

We improved some, but not all, of our financial metrics shown in Table 1. The improvement in our operating margin and surplus reflects the work undertaken to reduce costs across the business. Most significantly we have reduced our management costs per unit over the last four years by £352 in absolute terms, and by £500 when adjusted for inflation. Our maintenance costs per unit have been volatile during the period, and we have implemented an improved approach to asset management which we are confident will deliver the lower 2017 budget costs. Later in this report we set out more detail on our enhanced asset management strategy and how it will deliver savings. The budget for total maintenance spend for 2016/17 is £8.6 million lower than that for 2015/16.

Table 1: Financial metrics

	2017 Budget	2016	2015 (restated)	2014	2013
Operating surplus – social housing lettings (£'000)	36,470	41,348	35,330	25,889	28,242
Operating margin – social housing lettings (%)	30.6	32.9	30.1	24.2	26.1
Operating surplus per unit – social housing (£)	1,910	2,199	1,920	1,448	1,580
Management costs per unit – social housing (£)	1,140	1,179	1,147	1,330	1,531
Maintenance costs (including capitalised costs) per unit – social housing (£)	2,154	2,664	2,363	2,821	2,369
Operating costs per unit[1] – social housing (£)	4,324	4,482	4,448	4,530	4,468

[1]Total operating costs include management and maintenance costs, plus service charge costs, depreciation, and losses from voids.



A Catalyst colleague providing support to a customer

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Financial outcomes

Benchmarking our costs

We analyse our performance against the group of 15 large London providers of social housing (the g15), and against the sector average published in the HCA global accounts which is shown in Table 2. We have also considered our performance in light of the recent joint NHF/ HouseMark publication 'Housing association operational efficiency 2008/09 to 2014/15'.

Table 2: g15 and HCA global accounts benchmarked performance

Benchmarking our profitability	Catalyst 2016[1]	Catalyst 2015[2]	g15 2015 median	Catalyst g15 position	HCA 2015 global accounts
Operating margin – social housing	32.9%	27.1%	27.9%	3rd quartile	31.0%
Operating margin	30.5%	27.9%	Not published	Not published	28.3%
Net margin	32.1%	26.2%	Not published	Not published	18.5%
EBITDA MRI interest cover	146.1%	171.9%	171.9%	Median	28.7%
Debt per unit	£32,559	£32,064	£35,424	2nd quartile	£23,931

Benchmarking our costs	Catalyst 2016[1]	Catalyst 2015[2]	g15 2015 median	Catalyst g15 position	HCA 2015 global accounts
Management costs per unit	£626	£665	£589	3rd quartile	£1,034
Routine and planned maintenance per unit	£2,030	£1,991	£1,277	4th quartile	£1,240
Capitalised repairs per unit	£1,481	£1,465	£1,015	4th quartile	£705
Total maintenance and repairs per unit	£3,511	£3,456	£2,292	4th quartile	£1,945
Overheads as a percentage of turnover	9.8%	11.36%	11.91%	2nd quartile	19.9%
Rent loss from void properties	1.0%	0.7%	0.8%	7th	1.7%
Current tenant arrears	3.3%	3.4%	-	3rd	4.8%

[1]2016 numbers are estimated based upon our calculations using the HouseMark allocation process.
[2]Catalyst 2015 numbers are as included in 2014/15 g15 HouseMark report, prior to FRS 102 restatement.

Table 2 compares our latest 2016 results with the HouseMark 2015 g15 benchmarking report (the most recent available) on a like for like basis. The results show an improvement in our operating margin which has been below that of our peers in the g15 and the average from the HCA global accounts. We expect our improved operating margin for 2016 to compare more favourably when up to date benchmarking is completed, although we are aware that our peers have also sought to improve their performance.

A further area of attention for us is the spend per unit on repairs and maintenance, which has in recent years been much higher than our peers. Whilst we are confident that the quality of our stock has been enhanced by continued renewal and investment, we have also questioned whether we are spending wisely, often delivering standards which exceed our stated policy. Later in this report there are details of work completed to improve our asset management activities, and to improve our relative performance in this area. In the immediate future we have set a challenging maintenance budget for 2016/17, which demands savings of 25% over the prior year. This is based upon extensive analysis of the condition of our stock and restatement of the standards which we expect to achieve – no more, no less. We are therefore confident that this cost reduction is achievable without compromising Catalyst's letting standard.

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Financial outcomes

Headline social housing costs per unit

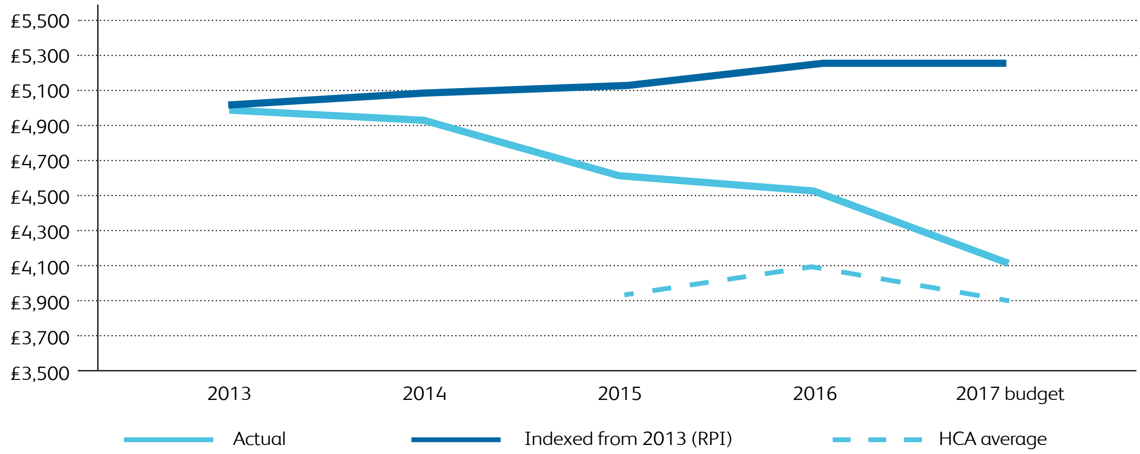
In June 2016 the HCA published their report 'Delivering better value for money: Understanding differences in unit costs'. Within it they define a 'headline social housing costs per unit' measure which aims to provide a robust and consistent measure of costs unaffected by individual providers' different approaches to accounting.

The new measure is made up of the main components of management, service charge costs, maintenance, major repairs and other social housing costs. It is a 'proxy cash' measure that excludes notional expenditure items – depreciation, impairment and bad debts – that are sensitive to different accounting policies and presentation of data within financial statements. It also excludes costs of sales and includes all major repairs, including those capitalised as well as expensed. All costs included in the measure are then divided by social housing units.

Within Chart 1 below we have used the HCA's definition to retrospectively calculate our headline social housing costs per unit over the last four years. We have also plotted the impact of RPI inflation from 2013 which shows our headline social housing costs per unit have decreased by over £1,100 in real terms over four years.

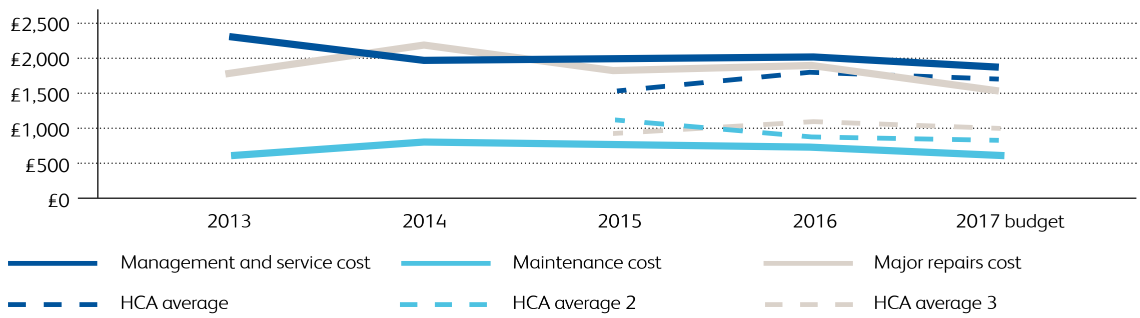
The HCA sector average headline social housing costs per unit for 2015, and forecasts compiled from regulatory returns for 2016, are also shown (as dashed lines) in the chart below. A comparison to our own results mirrors the findings from the benchmarking section above in that our costs are higher than our peers, and there is further work for us to do to reduce our costs. The fall in this measure in 2016 coupled with our continuing cost reduction strategy implemented within the 2017 budget demonstrates our commitment to ensuring that we improve our comparative position in future years.

Chart 1: Headline social housing costs per unit



In order to further analyse changes in headline social housing costs per unit we can disaggregate the component parts, as shown in Chart 2. The results show limited movement in each component over the four-year period. As above, the HCA sector average comparators for 2015 and forecasts compiled from regulatory returns for 2016 are also shown as dashed lines.

Chart 2: Disaggregated social housing costs per unit



The chart shows that for both management and service costs, and major repairs costs, our costs are above the sector average, but both are decreasing. Work is underway to reduce management costs through service transformation, and an improved asset management function will ensure the downward trend continues, as shown in the 2017 budget data.

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Service performance indicators

Making it Easy

The ‘Making it Easy’ customer service programme introduced last year continued to build momentum during 2015/16. We achieved most of the targets set for our service performance indicators, shown below in Table 3. We were disappointed with the overall satisfaction rating from the 2015/16 STAR survey which fell for the second year running. However during this time we embarked on a transformation of Catalyst to improve our services to customers, including significant leadership change and implementing a new structure which affected most of the Customer Service teams. We have now appointed a new Executive Director of Customer Services and have an ambitious digital strategy; and we are confident we have the foundations to deliver a sustainably high quality service that will have a positive impact on the satisfaction of existing and future customers of Catalyst.

Table 3: Service performance indicators

	2017 Target	2016 Actual	2016 Target	2015 restated	2014 restated
Residents’ satisfaction overall	80.0%	75.3%	80.0%	79.2%	80.6%
Bad debts – % of rental income	0.2%	0.3%	0.2%	0.2%	0.4%
Current arrears as a % of rent debit	3.0%	3.2%	4.5%	3.3%	5.9%
Rent loss due to voids	0.7%	1.0%	0.8%	1.3%	2.4%
Relet times (avg) – social housing	26 days	27 days	28 days	36 days	38 days
% of rent collection	101.0%	100.2%	101.0%	100.2%	101.2%
% of emergency repairs responded within target	99.0%	98.9%	98.0%	97.5%	99.4%
Gas safety compliance	100.0%	99.8%	100.0%	99.9%	99.5%

Triage neighbourhood service delivery model

We continued to embed our triage model for neighbourhood services and customer interventions. We completed 260 successful interventions during the year, which delivered £638,000 of benefit calculated in accordance with the HACT ‘Wellbeing’ value from an investment of £87,000.

Sustainability

We have achieved a number of improvements under our sustainability programme which deliver VfM by saving us money, and also deliver real savings to our customers. Highlights include:

- Maximising our income from energy feed in tariffs. Our income has grown to £14,000 per year and is still growing. We set aside one third of this for our Fuel Poverty and Sustainability Fund, which provides radiator panels, low energy bulbs and moisture traps for our most vulnerable residents. The remainder is passed on to residents through reduced service charges.
- We took part in the Big Energy Saving Network, a national project funded by the Department of Energy and Climate Change (DECC). We set a target to engage with 100 people, encouraging them to switch energy supplier, and trained 40 frontline employees in energy saving advice. In just four months we engaged with almost 300 residents about fuel poverty and energy saving, and identified potential savings of over £18,000 (as calculated by DECC).
- We apply the same sustainability principles to our facilities management, and have invested in LED lighting and other energy saving initiatives at our head office. We estimate that we’ve saved 37% on the cost of lighting our office. We’ve also transferred the provision of all our office energy to renewable energy tariffs and maintained the same unit price per kWh.
- We’re continuing to encourage behavioural change among our employees, we’re reducing our paper consumption, and have annual business mileage for the first time in five years.

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Return on assets

We measure the financial return on assets using a return on capital employed calculation of operating surplus over net book value. This measurement enables us to compare the returns across a number of tenure groups. The 2016 results by tenure are shown in Table 4 below, along with the equivalent results for 2015 (the net book values shown in the table reflect the implementation of FRS 102 accounting rules). The total return on capital employed for social housing lettings has improved year on year from 2.1% to 2.3%, reflecting our improving margin.

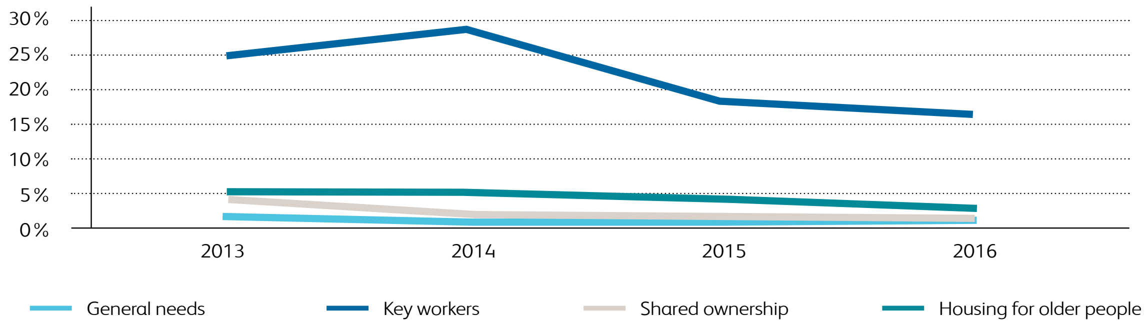
The fall in margin for older peoples' housing reflects an increase in planned maintenance works to a number of schemes during the year. We have completed a review of this area of our business and are considering a gradual withdrawal due to the low returns available from these assets, rising expectations and costs, downward pressure on fees and reputational risks. We will conduct our exit from these activities with care in order to protect the position of residents and employees as much as possible.

Table 4: Financial performance by tenure

	Turnover £million	Operating surplus £million	Operating margin	Net book value £million	Return on capital employed
2016					
Social rented – general needs, care & other	93.2	25.3	27.1%	1,433.2	1.7%
Key worker schemes	3.2	0.2	7.7%	32.0	0.8%
Supported and housing for older people	6.7	0.2	3.6%	38.7	0.6%
Shared ownership	22.5	15.6	69.4%	297.8	5.2%
Social housing lettings total	125.6	41.3	32.9%	1,801.7	2.3%
2015 (restated)					
Social rented – general needs, care & other	87.5	23.5	26.9%	1,314.7	1.8%
Key worker schemes	3.2	-	0.9%	30.2	0.1%
Supported and housing for older people	6.3	1.0	16.4%	64.4	1.6%
Shared ownership	20.2	10.8	53.7%	302.3	3.5%
Social housing lettings total	117.2	35.3	30.1%	1,711.6	2.1%

As well as the return on capital employed, we have also analysed the utilisation of our properties by tenure. Chart 3 below shows the void rates for each tenure type over the last four years. The chart shows the trend of our void rates falling over the period, and the overall void rate of 1% (Table 2) compares well with both the g15 peer group (0.8%) and the HCA global accounts for the sector (1.7%).

Chart 3: Void rate by tenure



Catalyst customers Jolanta Boho and family at home in Luton

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Asset management

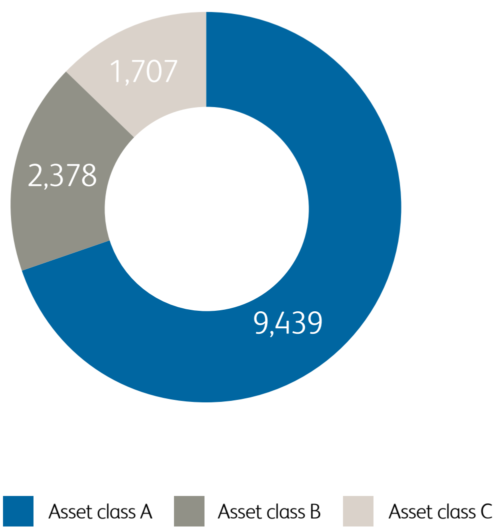
In our 2014/15 VfM report we set out our aim to improve our asset data. To enhance our understanding of our assets we have implemented a new asset management tool during the year, which will enable more accurate planning of periodic maintenance and improvement programmes. We have uploaded stock condition data to inform long term planning, and co-ordinated internal reviews of the data using both internal and external expertise. Savings from future programmes identified include:

- £10 million relating to external finishes and glazing that will not be required
- £10 million relating to assets that are poorly performing and falling into class C (see below)
- £3 million relating to assets where the responsibility for maintenance has transferred as a result of right to buy and other disposals.

During 2015/16 we have also completed work on our asset grading model for our social housing properties. The model grades assets using a number of tests based upon internal and external data sets, with class A being the highest performing; class B being higher performing, but requiring a higher level of investment; and class C being poorly performing and requiring significant investment, in some cases above a level which justifies continued retention. The classification methodology includes qualitative measures such as churn, ease of letting, ASB incidence, and quantitative measures such as actual income, historic costs and projected planned maintenance costs.

The outcomes form the initial grading process have been reviewed and are summarised in Chart 4 below.

Chart 4: Asset grading model outcomes



All the units within class C are either judged as not making a positive financial contribution to the business, or have failed further qualitative tests. There are a further 885 units within grade B which will fall at the lower end of the category. The next stage for these units is to carry out options appraisals for future use.

We expect to have completed options appraisals for these units during summer 2016, and will then form proposals into a combined programme of improvement works and selective disposals that ensures all of our properties reach a class A standard by 2020.

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Looking ahead

Our budget for 2016/17 requires us to sustain the savings achieved to date, and to further improve the efficiency of our repairs and maintenance service. We have reduced the combined capital and revenue budget on maintenance by 25%, a challenging target but one that our enhanced asset management data allows us to be confident of delivering. Savings in the region of 15% have been required from all other areas of the business, and we are concluding a number of restructures to ensure that we have the right people in the right roles to deliver our 2020 Vision. We are also looking to exit marginal and loss making areas of the business where these do not fit with our future priorities.

We want to ensure we remain a provider of good quality, value-for-money services to our current and future customers and we recognise that we are accountable for this to regulators, partners, and, most importantly, to our customers. We have established a Customer Experience Committee, the purpose of which is to recognise these various interests, and bring them together to ensure that we are continually adapting and improving our service offer and methods of provision. It is a committee of the Catalyst Board and as such it will take responsibility for the oversight of all customer related policies, practice and service outcomes, reporting back to the Board on issues of concern about the quality of the customer experience and making recommendations for any future changes to strategy, policy or practice.

Looking further ahead we will look to continue to drive down our operating costs whilst simultaneously improving service standards and satisfaction, adopting new ways of working and transferring services to digital platforms, and continuing to use our financial capacity to deliver more new housing for rent and sale. We believe Catalyst is delivering value for money across all activities, but have set out above the areas where further improvements will be delivered to keep pace with the change and meet future challenges.

A Catalyst shared ownership customer

CHL904 Catalyst 2016 AR FS Value for Money

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London W5 2AU

020 8832 3334
www.chg.org.uk

Registered Society
Registered Number: 16561R

Homes and Communities Agency
Registered Number: L0699

A charitable housing association

Front cover image: *Catalyst development, Wornington Green*

Catalyst

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