

Item

## Potential Expansion of Cambridge City Housing Company Limited

**To:**

Councillor Mike Davey, Executive Councillor for Finance, Resources and Transformation

Strategy & Resources Scrutiny Committee, 11 July 2022

**Report by:**

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**Wards affected:**

Abbey, Arbury, Castle, Cherry Hinton, Coleridge, East Chesterton, King's

### Key Decision

NOT FOR PUBLICATION: Appendix A to the report relates to an item during which the public is likely to be excluded from the meeting by virtue of paragraph 3 of Part 1 of Schedule 12A of the Local Government Act 1972. – ie. Information relating to the financial or business affairs of any particular person (including the authority holding that information).

### 1. Executive Summary

- 1.1 This report presents the findings from a project carried out between Cambridge City Council (CCC), Cambridge City Housing Company Ltd (CCHC) and Social Finance (a not for profit organisation who seek to tackle social problems in the UK and abroad).
- 1.2 The project has explored the potential for CCHC to expand its property portfolio by up to 250 homes over a 5 year period, offering affordable homes to lower income residents, living or working in Cambridge City, in an operationally efficient, cost effective and carbon neutral manner.
- 1.3 An initial feasibility study was carried out in the summer of 2021, with the positive findings from this early work prompting a more in depth project

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to be conducted. This project has however noted significant changes in the market assumptions since last summer, culminating in more cautious recommendations than initially hoped.

## **2. Recommendations**

The Executive Councillor is recommended, following scrutiny and debate at Strategy and Resources:

- a) To recognise that the proposed expansion of the CCHC portfolio by 250 new homes over the next 5 years, is not financially feasible at this time, in the current market conditions.
- b) To agree that CCHC keep the expansion metrics under review on a quarterly basis, reporting back to the Council, as shareholder, on an annual basis as part of the business plan update, unless a quarterly review results in a recommendation for moving forward with the expansion. If this is the case, a report will be presented to the Council for an expansion decision at the earliest opportunity.
- c) To authorise officers to explore in detail the potential for equity injection of an estimated £25 million, or a contribution towards the operating costs of the business, from partner organisations employing essential workers, in return for nomination rights to the homes acquired, presenting any proposals to the Council for consideration as shareholder.
- d) To agree that CCHC continues to explore expansion opportunities on a smaller scale, presenting independent funding requests for Council consideration and approval.
- e) To note that the Council, following a recent decision at Housing Scrutiny Committee, can now deliver some new affordable homes to be let at 80% of market rent, subject to award of Homes England Grant, to be managed within the Housing Revenue Account.

## **3. Background**

- 3.1 CCHC was incorporated on 15 February 2016, to alleviate some of the pressures on the intermediate housing market in Cambridge. The Company is an independent property company, wholly owned by

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Cambridge City Council, with a portfolio of 23 homes in the north of Cambridge.

- 3.2 In January 2019 the Council, as shareholder, moved the company from 'pilot' to a 'business as usual' status, with future expansion being an agreed area of exploration. Significant potential expansion was initially put on hold as a result of uncertainty in the market caused by Brexit, and then the coronavirus pandemic.
- 3.3 In the summer of 2021, the Council and Company were approached by Social Finance to undertake an initial 'pro bono' feasibility study for the potential to expand the property portfolio by up to 250 homes over a 5 year period, with the intention of letting homes at up to 80% of market rent, to lower income households who live or work in Cambridge. The proposal would have seen the Company acquire homes on the open market and carrying out initial works prior to letting them, but also investing in the homes over the life of the business plan to retrofit the homes, improving the energy efficiency, in line with Council commitments.
- 3.4 The initial feasibility study, which reported in August 2021, indicated that the expansion plan was worthy of more in depth exploration, and funding was incorporated in the General Fund Medium Term Financial Strategy to allow this to happen.
- 3.5 Social Finance were successful in securing the commission for this piece of work and began this in January 2022.
- 3.6 Social Finance conducted market research with prospective future tenants, explored the availability of suitable property in Cambridge, or the immediate travel to work area, reviewed and developed the eligibility criteria and lettings policy for the Company, reviewed governance arrangements for an extended portfolio, explored potential financing options, and undertook detailed financial modelling with updated market assumptions. The resulting report from Social Finance is attached as a confidential appendix to this report, due to the commercial sensitivity of the data.

- 3.7 Following the market research, Social Finance concluded that priority should be given to essential workers, on longer fixed term or flexible tenancies to provide security, with capped rent increases to provide the ability for residents to budget effectively. This would not preclude the housing being a viable option for others on low incomes who also live or work in Cambridge.
- 3.8 Between August 2021 and the finalisation of the detailed Social Finance potential expansion report, many of the market assumptions have shifted significantly, and unfortunately adversely. Over this period, inflation has risen at an unprecedented rate, interest rates have gone up, rent levels have not been maintained, and property prices have unexpectedly continued to increase. Maintenance costs have been reduced in percentage terms to be more comparable with the assumptions made by other housing providers, but it should be noted that material and labour prices are also fluctuating hugely currently, which may give rise to these assumptions needing to be returned to their initial levels. Retrofit is also currently cost prohibitive. The table below compares the initial key assumptions to those made as part of the final report.

<b>Key Assumption</b>	<b>Summer 2021</b>	<b>Spring 2022</b>
Acquisitions per year	50	50
Rent levels (percentage of market rent)	80%	80%
Borrowing interest rate	1.9%	3%
CPI inflation	2%	3.2%
Rent inflation	2%	3.2%
Acquisition cost – 1 bed	£200,000	£204,360
Acquisition cost – 2 bed	£275,000	£321,761
Acquisition cost – 3 bed	£400,000	£450,000
Acquisition cost – 4 bed	£553,000	£520,000
80% intermediate rent per week – 1 bed	£175	£166

80% intermediate rent per week – 2 bed	£235	£212
80% intermediate rent per week – 3 bed	£267	£246
80% intermediate rent per week – 4 bed	£350	£326
Management costs	8%	8%
Routine maintenance costs	10%	8%
Major repair costs	14%	12%

3.9 Using the revised market assumptions, expansion of the property portfolio is not considered financially feasible as this point in time.

3.10 The revised financial modelling assumes that the funding for the portfolio expansion is secured directly by CCHC through institutional investment, with the Council acting as guarantor or the loan (Option 4 below). This borrowing route has been incorporated due to the current uncertainty in the impact for the Council in terms of Minimum Revenue Provision (MRP) if the Council were to borrow and on-lend. At the time of writing this report, we await the outcome of a government consultation to confirm the position in this regard. If MRP is not deemed to be required, and the Council were to be able to borrow from the Public Works Loans Board (PWLB) and on-lend to the Company with any form of interest uplift, the rate would still be such that the expansion would be unviable when combined with the other market assumptions. The table below summarises the options explored by Social Finance.

<b>Financing Option</b>	<b>Description</b>	<b>Comment</b>
1 - PWLB maturity	CCC borrows and on-lends to CCHC on a maturity basis	Does not demonstrate financial viability for CCHC and carries MRP risk for the Council
2 - PWLB annuity	CCC borrows and on-lends to CCHC on an annuity basis	Not financially viable for CCHC and carries MRP risk for the Council

3 - CPI linked borrowing from institutional investors	CCC borrows from institutional investors based on CPI linked amortising borrowing	Nearest to being financially viable for CCHC, but carries MRP risk for the Council
4 - CCHC borrows with a CCC guarantee	CCHC borrows from institutional investors directly, with CCC providing a guarantee	Mitigates MRP risk for the Council, but does not demonstrate financial viability for CCHC

3.11 With expansion not financially feasible currently for CCHC alone, there are a number of suggested actions arising from the review, which include consideration of an injection of an estimated £25 million of equity amongst them:

- CCC / CCHC could explore partnerships with organisations which employ essential workers (such as Addenbrooke's), and who could inject equity, or subsidise the ongoing operational costs of the business, in return for accommodating their workforce.
- CCC could inject equity into the Housing Company, recognising that this could be subject to a satisfactory conclusion of the MRP consultation and the Council having available resource to invest.
- CCHC could review the financial metrics on a regular basis, to determine whether there have been changes in any assumption which move the potential expansion back into a position where it is considered financially feasible, alerting the Council to this as appropriate.

3.12 Although expansion of CCHC by acquiring existing homes on the open market is not currently financially feasible, a recent decision at Housing Scrutiny Committee does now allow the Council to build some new affordable homes to be let at up to 80% of market rent, subject to award of Homes England Grant, to be managed within the Housing Revenue Account. This will help to meet the housing need identified as part of this CCHC Expansion Project, whilst the above options are explored further.

## **4. Implications**

### **(a) Financial Implications**

The detailed financial assumptions, and the resulting impact for the Housing Company, are included in the attached appendix, which confirms that property portfolio expansion is not financially viable with the current market assumptions, without some form of equity injection or contribution towards the operational costs of the Company.

### **(b) Staffing Implications**

There are no direct staffing implications associated with this report.

### **(c) Equality and Poverty Implications**

There are no new equality or poverty implications associated with this report.

### **(d) Environmental Implications**

There are no new environmental implications arising from this report.

### **(e) Procurement Implications**

There are no new procurement implications arising from this report.

### **(f) Consultation and Communication**

As part of the work undertaken in this project, Social Finance consulted a variety of officers across the Council and interviewed a small representative sample of potential tenants for the proposed housing offering.

### **(g) Community Safety**

There are no community safety implications arising from this report.

## **5. Background Papers**

In preparing this report, officers referred to:

- Social Housing – Cambridge City Housing Company Acquisition Programme Feasibility Report.

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## **6. Appendices**

- Appendix A (Confidential) – Social Finance Report – Potential Expansion of Cambridge City Housing Company

## **7. Inspection of Papers**

To inspect the background papers or if you have a query on the report please contact:

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