UNAUDITED PRELIMINARY RESULTS

Year ended 31 March 2023

SOUTHERN HOUSING

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July 2023

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2024

CFO Summary

Sarah Smith Chief Financial Officer

MERGER UPDATE AND RESIDENT FOCUS

Southern Housing formed five months ago with the merger of Optivo and Southern Housing Group. Our new board keeps continuity with members drawn from both legacy businesses and our senior team is in place. Integration is going well and is on track to deliver its objectives. Residents are at the heart of our integration plans and strategy and we show this by co-creating our key decisions about policies, processes and systems with them. You can find our strategic plan here.

FINANCIAL SUMMARY 2022/23

At £73m our unaudited year end surplus is lower than last year's proforma comparative figure of £77m. This is partly because of impairment provisions, Year 1 merger costs including due diligence and professional fees before merger, writing off the two previous organisations' legacy capitalised loan set up fees at the point of merger and one-off integration costs after merger. These adverse movements were offset by fair value gains on financial instruments.

It also reflects a difficult operating environment with actual cost inflation exceeding CPI-linked income growth, slow open market sales countering good shared ownership sales, especially after the October mini-budget, rising interest rates on the small portion of our debt portfolio that's not fixed, and property impairment provisions. You'll find more details in later sections.

In spite of these challenges, our interest cover covenant performance remains above 200% and gearing below 50%. We have £1,480m total liquidity to cover £668m committed development expenditure.

ASSET MANAGEMENT

We are well advanced on our combined portfolio stock condition survey programme. We have updated our major repairs, building safety and decarbonisation cost estimates and these are now all costed into our new financial business plan.

DEVELOPMENT AND SALES ACTIVITY

We completed 1,178 homes last year against a target of 1,704, with 642 being for rent, 454 shared ownership and 82 open market sale. Our shared ownership sales remained good, but open market sales have been slower. Property fixed asset disposals have been challenging, especially in the London market.

OPERATING ENVIRONMENT

Cost pressures and rising stock investment needs have continued to squeeze our operating margins. The future is particularly challenging due to:

- Cost inflation exceeding rent inflation because of the 2023/24 rent cap
- Ongoing fire safety remedial actions and costs and new legal requirements
- Decarbonisation costs including Band C by 2030 and net zero by 2050.

Meanwhile the social housing grant environment hasn't yet changed to reflect the rising cost of delivering new social housing homes. Add to this the Bank of England base rate is at its highest level for 14 years and inflation has not yet abated; these are limiting factors to our development capacity.

We set our financial risk appetite metrics at merger and we're committed to staying within them. When we look at these against the backdrop of universally increasing costs we face inevitable compromises. So until we see compensating increases in grant availability across a range of housing activities, or a significant fall in land prices, some financial capacity we had previously set aside for building new social housing must now instead go to investing in our core housing stock. Regrettably this comes at the cost of growth.

SECTOR OUTLOOK

With the housing sector facing financial challenges, the Regulator of Social Housing has stated that some providers have had to obtain lender covenant waivers. We are not among those seeking any covenant waivers. However the pressures we're currently facing along with others are genuine.

We welcome the Levelling Up, Housing and Communities Committee inquiry into finances and sustainability in the social housing sector examining the financial pressures facing social landlords and the resources needed to meet a variety of challenges, including the need to build thousands of new homes for social rent and the task of improving social housing stock.

FINANCIAL RESILIENCE PLAN

While our lender financial covenants are comfortable, and our liquidity is strong, we have chosen to build our financial resilience further to withstand future uncertainties:

- While remaining firm in delivering all our existing commitments, we're significantly reducing the rate at which we'll commit to new developments
- We will increase the rate at which we dispose of homes that are no longer suited to our rental portfolio needs
- We will save £19.4m over the next three years through identified post-merger efficiency and then a further £14m by 2028/29, so reducing costs by 5%.

Implementing this financial resilience plan will support our strategic ambition to put residents at the heart of everything we do, to maintain safe assets which are good to live in, and to be a top performer amongst our peers for resident satisfaction.

OUR FUNDING AND ESG

We've established an ESG Programme Board of senior leaders across the business to ensure we remain at the forefront of sustainability reporting. We'll publish our next ESG Report to Investors in July.

We held investor roadshows in April to update our investors. The presentation used for these sessions is on our website.

2022/23 at a glance

		2021/22
Moody's rating	A3 (negative)	N/A
Fitch rating	A (stable)	N/A
Interim Regulatory judgements	G2/V2	N/A
Properties EPC C or better	73%	73%
People supported into jobs & training	2,081	1,379
Housing assets at cost	£5,810m	£5,539m
Total debt	£2,850m	£2,707m
Cash & cash equivalents	£146m	£188m
Operating margin excl sales	14%	20%
Total turnover	£644m	£592m
Operating surplus	£135m	£168m
Surplus after interest	£73m	£77m
New homes started	952	1,148
New homes completed	1,178	851
Capital commitments at year end	£668m	£528m
Weighted average debt duration	9.6 years	9.7years
Fixed rate debt proportion	88%	92%
Weighted average cost of debt	3.80%	3.72%
Available undrawn committed funding	£1,334m	£1,074m
Derivative fair value asset	£14m	(£21m)
No. of homes in contract	3,936	3,605

Financial performance

On 16 December 2022 Optivo and Southern Housing Group amalgamated to become Southern Housing.

Proforma figures for prior years have been prepared by combining the separate audited financial statements of Optivo and Southern Housing Group.

We have adopted the merger basis of accounting consolidation.

Income & expenditure (£m)	2020/21 Proforma	2021/22 Proforma	2022/23 unaudited
Total turnover	**544**	**592**	**644**
Rent, service charge & grant income	484	481	518
Shared ownership initial sales	50	64	60
Open market sales	10	47	66
Operating surplus	**165**	**168**	**135**
Operating margin excluding sales	21%	20%	14%
Surplus after interest	**74***	**77**	**73**

*Excluding 2020/21 gain on acquisition of Crown Simmons

Cashflows (£m)	2020/21 Proforma	2021/22 Proforma	2022/23 unaudited
Cash from operations	179	229	248
Investing activities	(167)	(282)	(305)
Financing activities	(86)	118	16
Net change in cash	**(74)**	**65**	**(42)**

Balance sheet (£m)	2020/21 Proforma	2021/22 Proforma	2022/23 unaudited
Total social housing assets (cost)	5,238	5,539	5,810
Total investment properties (valuation)	320	316	324
Total debt	2,482	2,707	2,850
Cash & cash equivalents	123	188	146

- Revenue increased due to delivery of new homes, despite construction delays
- Inflation impact on operating costs, higher asset management cost and merger implementation costs reduced our operating margin this year.
- Shared ownership sales continued to perform well in the year. Our initial sales surplus was £6.9m better than budget. Our sales programme is weighted towards shared ownership homes at 80% and open market sale at 20%.

Operating performance

General needs and HOPS key operational indicators	2020/21 Proforma	2021/22 Proforma	2022/23 unaudited
Void rental losses	1.1%	1.0%	1.1%
Overall rent arrears	4.4%	4.4%	4.7%

- Void turnaround times have held steady through the merger period.
- Arrears have risen slightly to 4.7%.
- We have increased our discretionary hardship fund to support residents facing cost of living challenges from £1.5m to £2m in 2023/24.
- In 2024, the Regulator of Social Housing will mandate us and other registered providers to report on Tenant Satisfaction Measures. Reporting on these measures will establish a consistent benchmark for assessing operating performance.

Property portfolio management

Expenditure (£m)	2020/21 Proforma	2021/22 Proforma	2022/23 unaudited
Routine maintenance	63	62	71
Planned maintenance	53	60	66

- We continue to keep a strong focus on all aspects of maintenance expenditure. Our first new post-merger financial plan has increased allowance for future building safety and decarbonisation costs, as well as catch-up works to improve stock condition.
- In line with the Better Social Housing Review we're working with key stakeholders to define the home data standards of the future. We'll ensure as an asset manager we "know our homes". We are proactive on damp and mould issues and we have a co-creation exercise with our residents, working together to improve our service and we have installed over 200 new damp meters to homes. We have surveyed 74% of our homes in the last 5 years and we have an active stock condition survey programme visiting 20% homes each year. We'll make well informed decisions and demonstrate we have good quality housing, meeting all regulatory standards and our residents' expectations.
- In March we acquired 794 homes in Surrey, Berkshire & Hampshire from L&Q increasing our concentration of properties in key geographical areas we serve.
- Fixed asset disposals have been challenging, predominantly in the London market, with a £6.4m shortfall against a £52m budget because of slowing sales at auction.

Property development & sales

New homes	2020/21 Proforma	2021/22 Proforma	2022/23 unaudited
Started in the period	1,141	1,148	952
Completed in the period	670	851	1,178
Sold in the period	430	502	403
In contract at the reporting date	3,469	3,605	3,936

Investment in new homes (£m)	2020/21 Proforma	2021/22 Proforma	2022/23 unaudited
Spent during the period	271	386	426
Future spend in contract	659	528	668

New homes available for sale at the reporting date	2020/21 Proforma	2021/22 Proforma	2022/23 unaudited
Open market sales	64	45	40
Unsold over six months	4	0	36
Shared ownership first tranche	404	238	257
Unsold over six months	164	114	59

- Despite all the financial pressures, having 3,936 homes in contract at the balance sheet date is a significant commitment that we have sufficient funding and liquidity to deliver.
- While development activity has been somewhat hampered by material and labour shortages, as well as cost increases putting suppliers under pressure, we have been completing projects and making new properties available for rent and sale.
- Forecasts of a property market slowdown continue to indicate a modest housing market correction. Though our shared ownership sales have progressed well.
- The increase in the number of our unsold homes in excess of 6 months old is due to the withdrawal of HelptoBuy and uncertainty in the market around interest rates and the impact of cost of living increases.
- Our 2022/23 unaudited results include impairment of £28m across 8 sites. Assessing the recoverability of sites necessarily requires a high degree of judgment. The provision made covers a land site held ahead of development where values have fallen, four schemes where sales values have been impacted by current market conditions and one site we anticipate will be subject to redevelopment.

Funding & liquidity

Funding sources (£m)	31.3.2021 Proforma	31.3.2022 Proforma	31.3.2023 unaudited
Listed own-name bonds			
Optivo Finance plc 2.857% 2035	150	250	282
Southern Housing 2.375% 2036	-	250	250
Southern Housing 4.500% 2039	75	75	75
Optivo Finance plc 5.250% 2043	150	250	300
Southern Housing 5.364% 2044	50	50	50
Southern Housing 3.500% 2047	300	300	300
Optivo Finance plc 3.283% 2048	250	250	250
Sub-total	**975**	**1,425**	**1,507**
Long-term finance aggregators			
The Housing Finance Corporation	191	179	178
Affordable Housing Finance	150	150	150
Other	36	14	13
Sub-total	**376**	**343**	**341**
Other facilities			
Bank term loans	715	581	606
Bank RCF drawings	218	300	349
Other	198	58	48
Sub-total	**1,131**	**939**	**1,003**
Total debt outstanding	**2,482**	**2,707**	**2,850**
Undrawn revolving credit facilities	1,042	1,074	1,334
Cash and cash equivalents	123	187	146
Total liquidity	**1,164**	**1,262**	**1,480**
Committed funding headroom:			
Available vs capital commitments	177%	239%	222%
Forecast next funding need	N/A	N/A	43 months

- The previous Optivo issuance vehicle, Optivo Finance plc, is now a wholly owned subsidiary of Southern Housing. We consider obligations of both Optivo Finance plc and Southern Housing as pari passu equally ranked with each other.
- We have over £1.5bn of own name bonds in issue, with maturities out to 2048. We have £68.5m of 2035 maturity retained bonds and £50m of 2036 maturity retained bonds available to sell in the future.

The 2036 maturity is our sustainable bond issued by Southern Housing Group in 2021. We'll publish an allocation and impact report this Autumn.

- Through amalgamation our lenders have increased their commitment to the enlarged group by some £200m.

As a result of prudent liquidity management and supportive lenders through our merger process last year, we now have ample liquidity. Now with a reducing rate of future development commitments, we are reviewing our overall liquidity level. At present our committed liquidity far exceeds our future requirements.

Interest rate risk management	2020/21 Proforma	2021/22 Proforma	2022/23 unaudited
Weighted average debt cost	3.86%	3.72%	3.80%
% of net debt on fixed basis	89%	92%	88%
Derivative mark-to-market	(£136m)	(£21m)	£14m
Duration	n/a	9.7 years	9.6 years

Lender financial covenant headroom	31.3.2021 Proforma	31.3.2022 Proforma	31.3.2023 unaudited
Total debt outstanding	£2,482m	£2,707m	£2,850m
Of which without corporate financial covenants:			
Long term publicly listed bonds	£975m	£1,425m	£1,507m
Other debt	£574m	£401m	£389m
Drawn debt proportion with no corporate financial covenants	62%	67%	67%
Interest cover headroom vs test threshold			
Actual interest cover (lender threshold > 125%)	206%	221%	202%
Earnings could fall by	£86m	£99m	£80m
Interest expense could rise by	£75m	£86m	£64m
Gearing headroom vs test threshold			
Actual gearing (lender threshold< 70%)	44%	46%	49%
Debt could rise by	£1,150m	£1,104m	£1,337m
Assets could fall by	£1,769m	£1,698m	£1,910m

- We fix our debt costs using a combination of fixed rate debt instruments and floating rate debt backed by standalone interest rate derivatives. Our standalone derivatives mark to market has changed from liability to asset due to rising interest rates. All our derivative lines remain well collateralised in case of a return to low rates.

- Two-thirds of our drawn debt is not subject to financial covenants.

- Where our debt does have lender covenants, we are satisfied there is sufficient headroom for our needs.

About Southern Housing

Southern Housing is registered in England with limited liability under the Co-operative and Community Benefit Societies Act 2014 (registration number 8983) and is a Registered Provider of Social Housing whose activities are regulated by the Regulator of Social Housing (registration number 5171). Southern Housing has charitable status but is exempt from registration with the Charity Commission.

About Optivo Finance PLC

Optivo Finance plc (company number 07933814) is a wholly owned subsidiary of Southern Housing and issuer of secured bonds listed on London Stock Exchange, whose net proceeds it on-lends to Southern Housing for its general corporate purposes.

Bloomberg ticker

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Important Note

This publication contains certain 'forward-looking' statements reflecting, among other matters, our current views on markets, activities and prospects. Actual outcomes may differ materially. Such statements are a correct reflection of our views only on the publication date and no representation or warranty is given in relation to them, including as to their completeness or accuracy or the basis on which they were prepared. Financial results quoted are unaudited. No reliance should be placed on the information contained within this update. We do not undertake to update or revise such public statements as and when our expectations change in response to events. This publication is neither recommendation nor advice.
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