Mid Year Business Update

November 2016

Making homes and lives better
wheatley-group.com

Wheatley Group

Executive Summary

2015/16 was another year of significant growth, diversification and continued strong financial performance.

Two new partner organisations, both with substantial footprints in the east of Scotland, have recently been welcomed into the Wheatley family. The highly respected Dunedin Canmore Group, with almost 6000 affordable homes in Edinburgh, the Lothians and Fife, joined at the beginning of the financial year; and Barony, one of Scotland's leading care providers supporting over 700 people from Edinburgh and the Lothians to Stirling and Falkirk, became the latest addition to the Group, joining Wheatley on 1 April 2016.

It means Wheatley now operates across 17 local authorities and we continue to increase the supply of much-needed affordable homes and provide award-winning housing, care and property management services to almost 200,000 customers.

Excellent progress continues to be made on the ongoing implementation through to 2020 of our five-year strategy, 'Investing in Our Futures'. This is built around five pillars, all of which were shaped and influenced by the feedback of our tenants, the people we work for in care, YourPlace's 27,700 factored homeowners and our 2,300 staff.

They are:

- customer service excellence;
- growing our assets to provide more affordable housing;
- transforming the care environment;
- building the capability of our people;
- establishing a strong and diverse funding base.

The strategic partnerships forged with several local authorities, including Glasgow and Edinburgh City Councils and West Dunbartonshire Council, provide solid foundations on which we are playing our part in addressing the acute demand across Scotland for social and mid-market homes. Wheatley's £300 million debut public bond issuance in late 2014 enabled the completion of 721 good-quality, affordable homes, with an additional 888 in construction and a further 1,528 in development.

Strong financial management and performance throughout the year saw us outperform our revenue budget by over £2 million, realising an operating margin of 52% and a surplus after interest and tax of £111 million. The Group is in a healthy financial position and is well-placed to adapt to any challenges which may arise following the UK's vote in June 2016 to leave the European Union.

And the first half of this year has proven to be equally active.

The integration of Barony into the Group is well into the mobilisation phase with the co-location of the Barony and Dunedin Canmore teams into the same office. Dunedin Canmore itself is moving into a transformation and integration stage, now approved by their Board, and this will be progressed in the second half of the year.

The establishment of a new joint venture arrangement with Glasgow City Council to provide an integrated repairs and maintenance service through joint ownership of City Building (Glasgow) is in the process of being finalised and will be in place for the start of the 2017/18 financial year. This will transform our approach to the delivery of our reactive and planned maintenance service and leverage the synergies and flexibility that come with integration of this key supply partner. This new partnership supplements a new strategic agreement with Glasgow City Council which continues the strong relationship and shared objective of delivering further affordable homes across the city.

In addition, a new structure to deliver internal services across the Group has been established with the incorporation of Wheatley Solutions – this approach brings service delivery teams together to ensure a consistent, efficient, and high quality approach to the business of providing in-house services.

Externally, the markets we work in also continue to experience rapid change. The UK 'Brexit' vote has led to significant financial market uncertainty and has re-opened the debate as to whether a second Scottish Independence Referendum should be held. Neither of these debates is likely to have a short term conclusion and we have undertaken specific business plan risk modelling to ensure that the organisation remains financially robust under a range of potential scenarios.

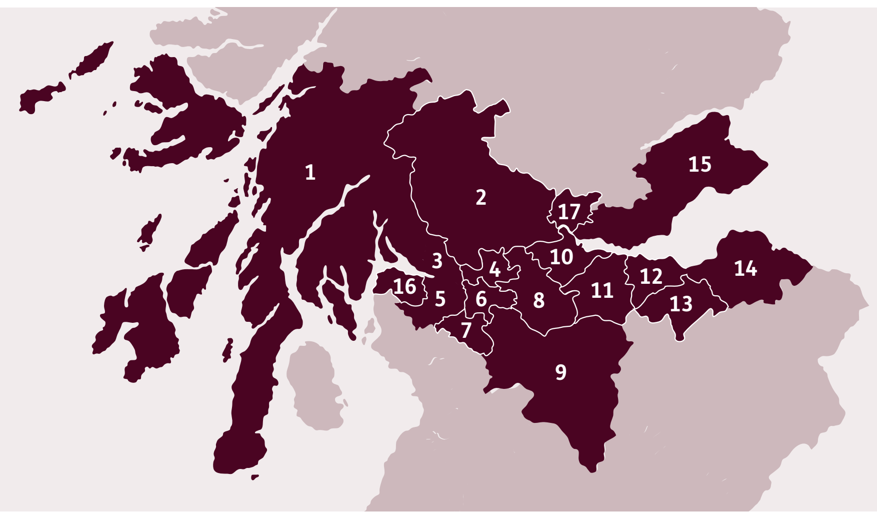
Alongside this, the Office of National Statistics has reclassified the Social Housing Sector as 'public sector' and, whilst this does not bring immediate implications, the regulatory regime will evolve in response to this decision. The Scottish Government has been very clear in its intent to keep the social housing sector off the public sector balance sheet to ensure that the benefits that can accrue from leveraging private finance alongside public sector investment are maintained. A Housing Bill is to be brought forward to ensure that an appropriate package of measures is put in place to achieve this aim – this is expected to largely mirror the approach being taken in the Housing and Planning Act 2016 in England. We will continue to work closely with the Scottish Housing Regulator to ensure that we adapt to any changes that are forthcoming, if required.

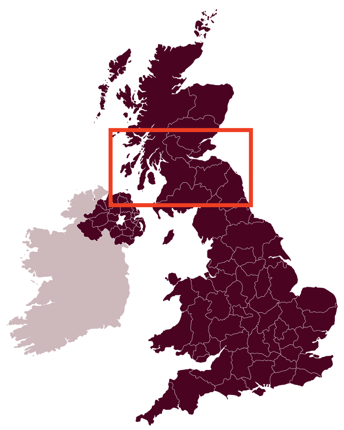
Our financial performance in the six month period to 30 September 2016 has been strong, delivering results in line with expectations. We have continued to deliver our commitments to our existing homes with a £32.6m investment in the first half of the year, this being complemented by our wider new build development strategy where we had 683 new homes approved by our RSL Boards and 100 more projects in the forward pipeline. Our full year plans deliver turnover of £271.6m generating an operating surplus of £51.5m, at a margin of 19%.

683
number of new homes approved by our RSL Boards

Who we are and where we operate
The completion of the partnership with Barony in April 2016 extended Wheatley's operational footprint to 17 of the 32 local authority areas across central Scotland.

Wheatley Group footprint





1 Argyll and Bute
2 Stirling
3 West Dunbartonshire
4 East Dunbartonshire
5 Renfrewshire
6 Glasgow City
7 East Renfrewshire
8 North Lanarkshire
9 South Lanarkshire
10 Falkirk
11 West Lothian
12 City of Edinburgh
13 Midlothian
14 East Lothian
15 Fife
16 Inverclyde
17 Clackmannanshire

The Group's operational entities are:

Seven Registered Social Landlords:

- *Wheatley Housing Group Ltd ("Wheatley") – the Group parent does not own any homes, but is registered with the Scottish Housing Regulator and is responsible for providing strategic direction, and oversight for the Group*
- *The Glasgow Housing Association Ltd ("GHA") – Scotland's largest Registered Social Landlord, with 39,235 homes in Glasgow (excluding properties classified for demolition)*
- *Cube Housing Association Ltd ("Cube") – with 3,438 properties across the west of Scotland*
- *West Lothian Housing Partnership Ltd ("WLHP") – which owns and manages 381 affordable homes in West Lothian*
- *Loretto Housing Association Ltd ("LHA") – a specialist provider of supported accommodation with 1,290 properties in west and central Scotland*
- *Dunedin Canmore Housing Ltd ("DC") – with 5,640 affordable rented properties across Edinburgh, the Lothians and Fife*
- *Barony Housing Association Ltd ("Barony") – which has 361 homes and provides care and support to over 700 people from Edinburgh and the Lothians to Stirling and Falkirk.*

A charitable care provider, Loretto Care, which supports over 2,000 people with specialist needs, many of whom live in properties owned by its parent entity, Loretto Housing Association Ltd

Three commercial entities:

- *YourPlace Property Management Ltd – providing factoring (common property management services) to over 27,700 customers*
- *Lowther Homes Ltd – with 517 private rented homes; it also provides management services for the Group's mid-market rented homes*
- *Dunedin Canmore Enterprise – with 127 properties, the majority of which are for mid-market rent, and providing property management and repairs and maintenance services to Dunedin Canmore Housing.*

In April 2016, two new entities were established within the Wheatley Group, being:

- *Wheatley Foundation Ltd – the new provider for our community and better lives activity*
- *Wheatley Solutions Ltd – to provide a clear focus for our group support services and business services (such as finance, legal, HR and ICT) to subsidiaries across the Group.*

Wheatley's position as a Scottish landlord
Wheatley Group, as by far the largest housing group in Scotland (five times larger than the next largest), is of systemic importance to the Scottish housing sector. We continue to have a high level of engagement with the Scottish Housing Regulator and Scottish Government.

Standard & Poor's have refreshed their credit rating assessments of their UK RSL portfolio a number of times during the year which is reflective of the movements in the wider political landscape. In their October 2016 rating report for Wheatley they noted that:

"...the rating affirmation [at A+] reflects... our view of an extremely high likelihood of Wheatley receiving extraordinary support from the Scottish government in the event of financial distress; and Wheatley's relatively large size compared with its housing association peers in Scotland.

Wheatley's critical role reflects its central and systemic importance within the Scottish social housing sector. The Scottish government describes it as "a key delivery partner", with Wheatley set to deliver a minimum of 10% of the government's plan of building 50,000 affordable homes over the next five years."

The impact of external factors in the ratings can be evidenced through the rating movements in the six months to September 2016.

Wheatley obtained a one notch upgrade to AA in June 2016, which was subsequently reduced by 2 notches in July 2016 following the 'Brexit' vote. This reflects Standard & Poor's view on the new macro-economic systemic risks that exist as a result of this vote and all rated Housing Associations across the UK were downgraded in July.

Wheatley currently benefit from an allocated A+ (negative outlook) rating which is in line with the majority of our English Peer group.

The potential impact of Welfare Reform
The changes under Welfare Reform will be hugely important to our tenants, our customers, and our own organisation. We have looked in detail at how widespread the impact might be to ensure that we understand and are able to support those who are affected. At present 700 of our tenants are on Universal Credit and the Scottish Government has committed to using its devolved welfare powers to continue the payment of the housing benefit element of universal credit direct to the landlord. The benefit cap, which has reduced from £26,000 to £20,000, will initially affect around 600 of our households and this is likely to increase by nearly 300 new households per year. Our expectations are that the Scottish Government will work to mitigate the effect of the Local Housing cap through their devolved statutory powers. In addition, we are changing our housing policies to minimise the risk to future tenants of living in housing they cannot afford and our business planning ensures that conservative assumptions in relation to bad debt levels are built in.

Scottish social housing – increasing divergence from England
The Scottish social housing sector is distinct from that in England in a number of important ways. Housing, including social housing, has been a matter devolved to the Scottish Government since 1999. Reflecting the political make-up of the Scottish Parliament, which is left-of-centre, social housing has consistently been a high political priority, and one which has spanned successive administrations, regardless of the parties involved.

Social housing is more prevalent in Scotland than England, comprising almost 24%[1] of all Scottish housing stock , compared to 17% in England[2]. Scotland has a slightly lower rate of owner-occupation than England, 58%[1] compared to 64%[2]. The proportion of housing in the private rented sector is 15% in Scotland[1], compared to 19% in England[2]. This has been reflected in the nature of Scottish Government legislation on the issue, which has increasingly diverged from England in recent years. These differences have grown significantly since the UK Government Budget in June 2015, as highlighted in the table below:

1 http://www.scotland.gov.uk/Topics/Statistics/Browse/Housing-Regeneration/HSfS/KeyInfoTables (updated after Scottish Household Survey 2015 was published) 23.3% of housing stock in Scotland is socially rented. Of this 10.9% are rented by Registered Social Landlords and 12.4% by Local Authorities.

2 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/501065/EHS_Headline_report_2014-15.pdf

	England	Scotland
Rent cut	1% rent cut imposed by central Government for next 4 years.	**No rent cuts in Scotland** – housing associations are free to set rents with no central government rent controls or caps and Scottish Ministers have confirmed that this will continue to be the case.
Right To Buy	Being extended to housing associations.	**Abolished in Scotland** by the Housing (Scotland) Act 2014.
Pay to stay	Tenants on higher incomes in England will be required to pay market rate, or near market rate, rents.	**No pay-to-stay requirement** in Scotland.
Universal Credit	Being rolled out and will include housing benefit. Introduces risk of individuals paying their rent for the first time and consequent risk of increase in arrears and bad debts.	Devolution legislation provides the Scottish Government with powers to direct the **continued payment of housing benefit straight to social landlords** – mitigating the impact of Universal Credit.
Grant support for new build	Social housing not supported by the HCA through new build grant. S106 planning requirements for social housing being scrapped – reduced pipeline of schemes for social landlords.	New build **grant levels significantly higher than England** (benchmark £72,000 per unit and proposals to increase this) – with ongoing **cross-party support for new affordable housing.**
Bedroom tax	Applies in full – reduces housing benefit entitlement and increases payment/income risks to housing associations.	**Bedroom tax effectively abolished** in Scotland through Scottish Government subsidy, with devolution proposals likely to formalise this.
Diversification model	Move to higher risk business areas such as build for sale housing and other property development activity.	More **traditional, low risk business model** based on government-backed revenue streams; minimal reliance on commercial income such as build for sale, or exposure to the care sector.

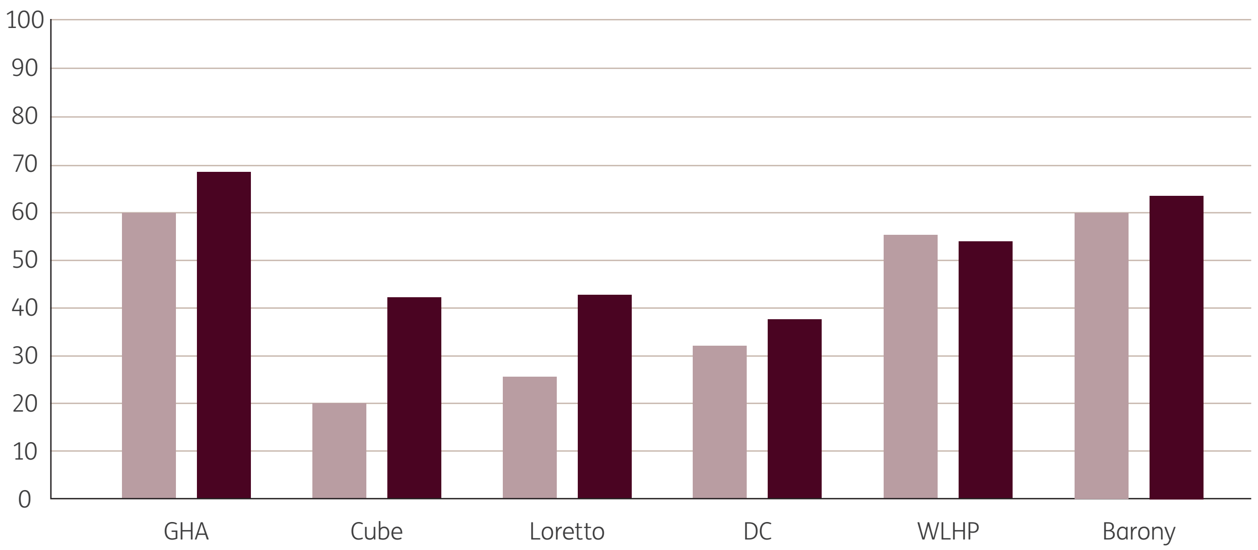
Performance overview

Registered Social Landlords (RSLs)
The 2015/16 Annual Returns on the Scottish Social Housing Charter showed that all but one of our housing associations increased their number of top quartile performance indicators during 2015/16. Over half of all GHA, West Lothian Housing Partnership and Barony indicators are in the top quartile in Scottish terms.

Percentages of 2015/16 indicators in the top quartile in performance terms in comparison with 2014/15 Scottish Social Housing Charter returns

Percentages of 2015/16 indicators in the top quartile in performance

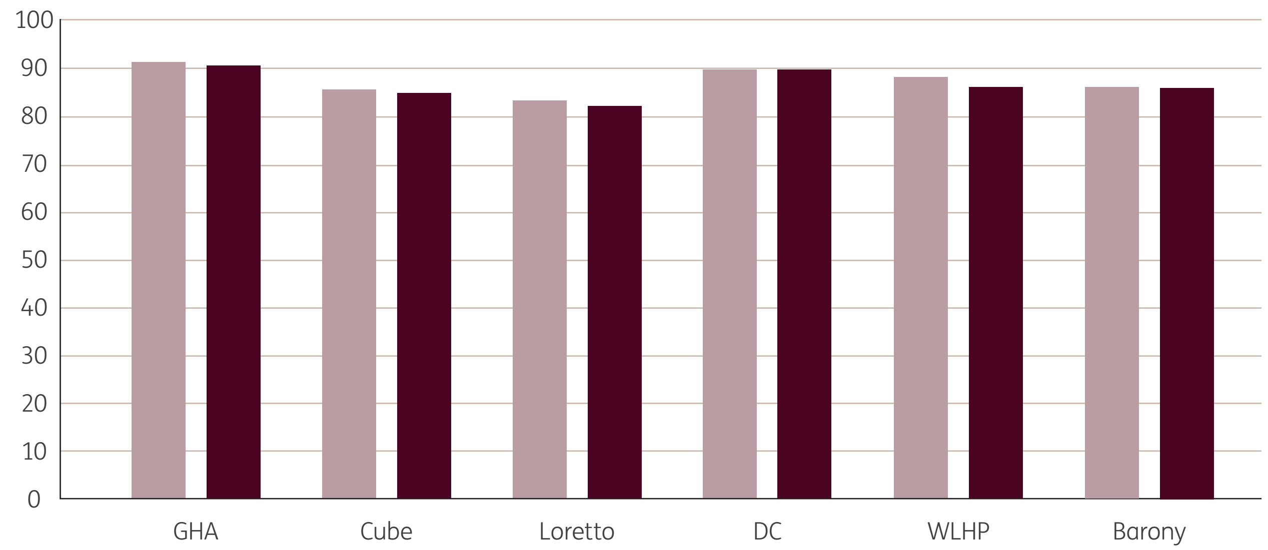
2014 – 15   2015 – 16



A drive to maintain outstanding customer satisfaction is at the heart of our approach to performance. The chart below illustrates the consistently strong level of satisfaction across all of our housing association subsidiaries:

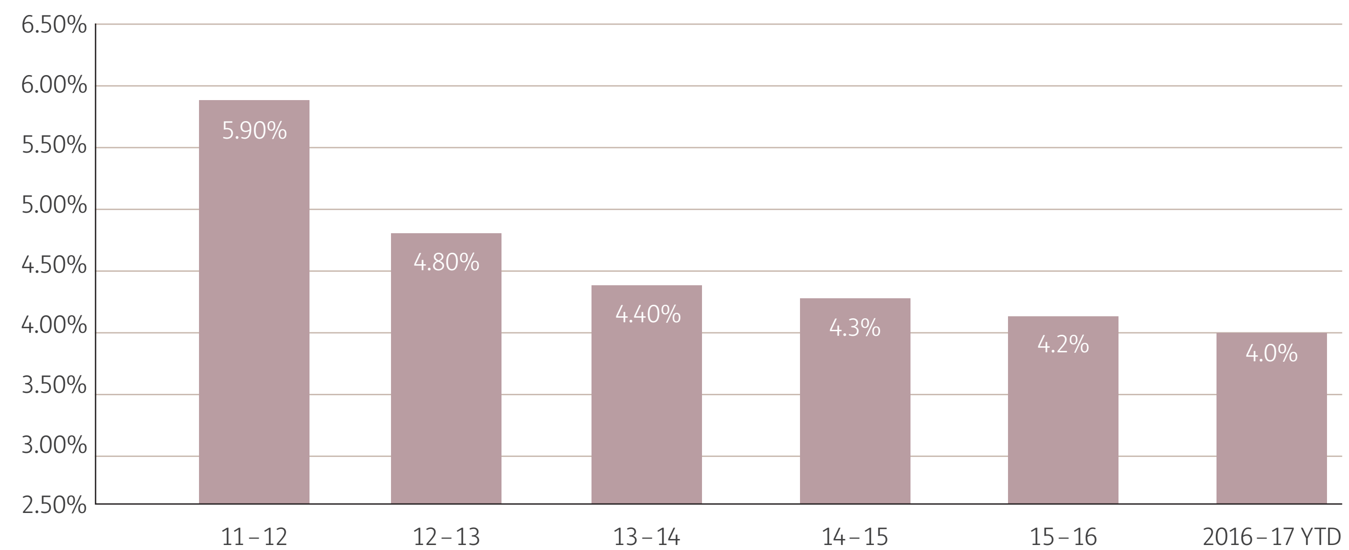
Consistently outstanding customer satisfaction

2014 – 15   2015 – 16



The charts below show positive performance in relation to arrears, and days to let vacant properties, across the Wheatley Group:

Overall rent arrears (current and former tenants)



Source: Scottish Social Housing Regulator returns; 2016/17 YTD position as at 30 Sept 2016

Average days to let vacant properties

Source: Scottish Social Housing Regulator returns; Wheatley figures stated as weighted average of Group RSLs

Commercial subsidiaries

In 2015/16 YourPlace returned just under £1.3 million in Gift Aid to the Group, to be invested back into our communities, exceeding its target of £0.9 million. As part of Wheatley Group's Investing In Our Futures strategy, YourPlace aims to deliver factoring services to an additional 5,000 homes by 2020, offering a wide range of services to customers across the west of Scotland. During 2015/16, YourPlace increased its factored stock by 2,065 properties.

YourPlace has also secured the position as factor for a number of developments which are currently under construction. This will bring on a further 1,492 properties by 2018.

The excellent business performance of Lowther Homes, which has a growing portfolio of 700 owned and managed properties, ranged from an average of 19 days to let a home, against a target of 27, to a void rate of 2.2% against a target of 3%.

Financial performance
A three-year summary of the Group income and expenditure and balance sheet is set out below:

Statement of Comprehensive Income	**2014–15**	**2015–16**	**2016–17**
	Actual	***Actual***	***Forecast***
	£000	***£000***	***£000***
Turnover	252,183	281,157	271,557
Operating expenditure	(217,553)	(235,646)	(231,357)
Other income and gains	8,237	101,981	11,332
Operating surplus	**42,867**	**147,492**	**51,532**
Operating margin %	**17%**	**52%**	**19%**
Gain on disposal of fixed assets	2,183	2,817	3,214
Net finance costs	(35,270)	(47,782)	(53,606)
Movement in fair value of financial instruments	2	9,265	0
Surplus before tax	**9,782**	**111,792**	**1,140**
Taxation	(34)	(642)	0
Surplus for the year	**9,748**	**111,150**	**1,140**

The year to 31 March 2016 saw a continued strengthening of financial performance across the Wheatley Group. From a turnover of £281.2m (2015: £252.2m), the Group achieved an operating surplus of £147.5m, at an operating margin of 52.5%. This outturn benefited from gains on business combinations of £103.3m reflecting the new partnership with Dunedin Canmore who joined the group in the year and an underlying operating surplus of £45.5m was delivered at a margin of 16.2% (2015: £34.6m and 13.7%).

Total Comprehensive Income for the year of £130.5m (2015: £71.2m) reflected the operating surplus combined with the improving position of the Group's pension schemes. A continued focus on efficiency and value for money delivered an operating margin from social lettings of 33%.

Income from non-social housing sources continued to represent a relatively small proportion of the Group's activity in financial terms. Loretto Care, the Group's care and support subsidiary, reported turnover of £13.8m (4.9% of Group turnover) and posted a surplus of £0.1m, while income from investment/commercial property was £11.1m (4.0% of Group turnover).

For the six months to 30 September 2016, turnover at £131.7m is in line with plan and is anticipated to translate into a full year forecast of £271.6m. Operating surplus of £17.4m for the half-year is forecast to grow to £40.2m for the full-year, at an operating margin of 14.8% before gains on business combinations are taken into account; including the gain on business combinations, from Barony (£10.1m), forecast surplus is £51.5m, at a margin of 18.5%.

The benefit of Barony joining the group has exceeded budget by £4.1m reflecting a prudent approach to budgeting for this partnership and will contribute to a strong full year financial outturn.

Statement of Financial Position	2014–15	2015–16	2016–17
	Actual	*Actual*	*Forecast*
	£000	*£000*	*£000*
Housing and investment properties	1,241,320	1,604,950	1,706,785
Other fixed assets	22,644	30,488	34,030
	1,263,964	**1,635,438**	**1,740,815**
Pension asset	10,684	31,432	31,432
Stock	0	263	0
Trade and other debtors	146,144	132,714	105,612
Cash and cash equivalents	101,996	61,691	90,767
	248,140	**194,668**	**196,379**
Creditors <1 year	(97,312)	(86,115)	(99,959)
Net current assets	**150,828**	**108,553**	**96,420**
Creditors > 1 year	(762,878)	(997,147)	(1,111,785)
Pension liability	(7,831)	(7,428)	(8,450)
Provisions for other liabilities	(117,262)	(102,804)	(79,248)
Net assets	**537,505**	**668,044**	**669,184**
Revenue reserves	466,322	603,900	605,040
Revaluation reserve	71,183	64,144	64,144
Total reserves	**537,505**	**668,044**	**669,184**

The Group Statement of Financial Position at 31 March 2016 showed an increase in the value of housing properties during the year of £363.6m (29%), reflecting the acquisition of Dunedin Canmore and the on-going benefit of the investment we make in customers' homes and our new build programme. Capital and reserves have grown by 24% to £668.0m, giving us a strong platform for investment in growth and new development. The Group has net pension assets, in contrast to many of our peers who are managing significant pension liabilities.

Debt levels remain prudent and sustainable. Long term housing loans in the Statement of Financial Position were £936.9m (2015: £731.0m) with gearing, based on the prudent measure of net debt / balance sheet property values (with social housing assets valued at Existing Use Value – Social Housing), of 56%. Gross debt per unit was £16,695 which is below the majority of large UK housing groups.

We manage our business within a number of 'Financial Golden Rules' which are reviewed annually by our Group Board and are set out below. These were all comfortably met at 30 September 2016.

Golden Rule	Description
Liquidity	Cash requirement for next 12 months + 25% contingency to be met through available cash and undrawn debt capacity
Contracted Development	Contracted development + 25% contingency to be covered by cash and available facilities
Gearing	Net debt/asset valuation for RSL borrower group not to exceed 75%
Gross Debt Per Unit	Not to exceed £25,000 across RSL borrower group
Interest Cover	Adjusted operating surplus (adding back depreciation, new build grant, and RTB gain on sales) to be greater than or equal to 1.2x across RSL borrower group

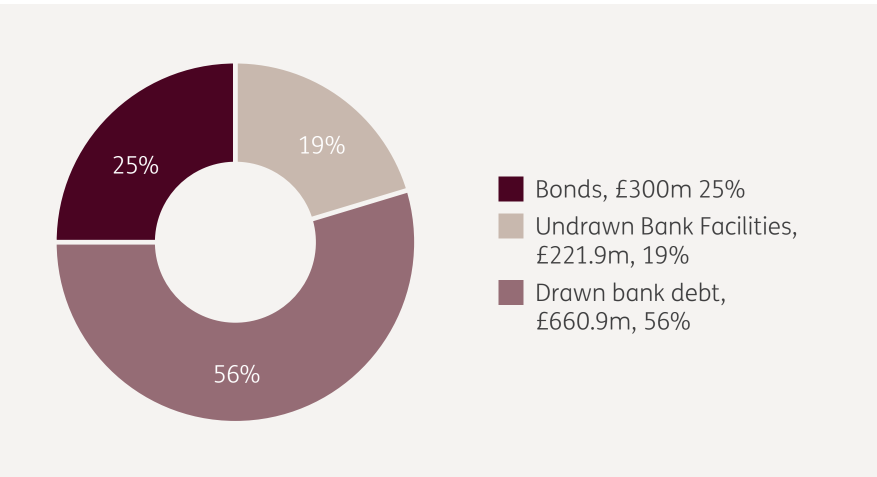
Cash flow and liquidity
The Group Cash Flow Statement for 2015/16 demonstrated a strengthening operating cash flow. Net cash inflow from operating activities was up by 56% to £70.7m (2015: £45.4m).

The Group's strong liquidity position is further supported by its continuing annual access to grant income under long-term agreements with the Scottish Government, of which £20.1m was drawn down during the year (2015: £37.6m). Cash of £61.7m was held at 31 March 2016.

Strong liquidity and low refinancing risk
At 30 September 2016, the Group had £1,182.8m of bond and bank funding facilities in place, with two funding vehicles supporting the business: Wheatley Funding No. 1 Ltd ("WFL1") provides funding facilities to a number of the RSLs, secured on core RSLs assets, whilst Wheatley Funding No. 2 Ltd ("WFL2") supports the operations of the commercial subsidiaries within the Group, secured on assets of Lowther Homes Limited, Dunedin Canmore Enterprise and a number of Dunedin Canmore Housing properties. The funding facilities in place on 30 September 2016 comprised the following:

Group Co	Facility	Principal
WFL1	Public Bond	£300.0m
	Commercial bank syndicated facility	£669.0m
	European Investment Bank facility	£132.5m
DCH	THFC facility	£16.5m
WFL2	Private rented sector bank finance	£59.8m
Cube	SPRUCE (Unsecured) loan facility	£5.0m
		£1,182.8m

Nineteen per cent (£226.9m) of the Group's borrowing facilities were undrawn at 30 September 2016:



The weighted average duration of drawn debt across the Group is 19.8 years. Under the Group Treasury Management Policy, the Group structures its business plan and future fundraising activities such that it will not have to refinance material amounts of debt in any one year. None of the Group's loan facilities need to be refinanced over the next five years. The next point of significant refinancing risk will arise in 2021/22 in relation to £50m of bank loan facilities for the Group's commercial subsidiary, Lowther Homes. The historic weighted average cost of drawn debt, inclusive of margins and hedging activities, was 5.33% at 31 March 2016, on an annual effective rate basis (2015: 4.98%).

The principal cash outflows during 2015/16 were operating costs and investment in assets, particularly in development of new housing stock of £52.6m (2015: £71.9m) and investment in existing stock of £73.1m (2014: £51.8m).

Financial Projections
Looking forward, our financial projections reflect the continued stable and robust group business model. Our revenue base develops in line with our sustainable new build programme, and our rental income is underpinned by a strategy which balances the financial needs of our tenants with our overall objective to continue to provide a high quality of living space.

Our operating cost base remains in focus. We will continue to see a containment of costs as we complete some of our priority regeneration programme, and costs associated with our demolitions schemes come to an end. Our cost investment in assessing the potential impact of Welfare Reform to our tenants and ourselves is now largely complete and whilst we now hope that the majority of the impact will be mitigated by Scottish Government supplementary support the work undertaken has helped develop a wealth of knowledge about our tenants which we can use to tailor our services for the future.

In summary, we look forward to taking the business forward, built on the existing strong platform, and continuing to develop a strong and stable operating margin on which to deliver further services for our tenants in the future.

Statement of Comprehensive Income	**2017/18**	**2018/19**	**2019/20**	**2020/21**	**2021/22**
	£000	***£000***	***£000***	***£000***	***£000***
Turnover	301,522	317,238	322,706	321,626	329,059
Operating expenditure	(227,643)	(222,907)	(228,462)	(234,912)	(240,834)
Other income and gains	191	(603)	19	1,497	3,711
Operating surplus	**74,070**	**93,728**	**94,264**	**88,211**	**91,936**
Operating margin %	**25%**	**30%**	**29%**	**27%**	**28%**
Net finance costs	(62,185)	(61,552)	(68,544)	(73,565)	(75,273)
Surplus before tax	**11,885**	**32,175**	**25,719**	**14,646**	**16,662**
Taxation	(105)	(324)	(299)	(236)	(198)
Surplus for the year	**11,780**	**31,852**	**25,420**	**14,410**	**16,465**

Statement of Financial Position	2017/18	2018/19	2019/20	2020/21	2021/22
	£000	*£000*	*£000s*	*£000s*	*£000s*
Housing and investment properties	1,868,919	1,957,450	2,016,118	2,057,011	2,081,529
Other fixed assets	22,054	21,158	19,832	19,268	18,378
	1,890,973	**1,978,607**	**2,035,950**	**2,076,279**	**2,099,907**
Pension asset	31,432	31,432	31,432	31,432	31,432
Trade and other debtors	50,124	50,146	49,408	49,623	49,809
Cash and cash equivalents	91,998	101,358	98,686	59,518	41,056
	142,121	**151,504**	**148,095**	**109,141**	**90,865**
Creditors <1 year	(115,540)	(103,204)	(83,811)	(78,764)	(72,176)
Net current assets	**26,582**	**48,300**	**64,283**	**30,377**	**18,689**
Creditors >1 year	(1,260,858)	(1,338,359)	(1,386,265)	(1,378,278)	(1,373,753)
Pension liability	(8,450)	(8,450)	(8,450)	(8,450)	(8,450)
Provisions for other liabilities	(3,198)	(3,198)	(3,198)	(3,198)	(3,198)
Net assets	**676,481**	**708,332**	**733,753**	**748,163**	**764,628**
Reserves	**676,481**	**708,332**	**733,753**	**748,163**	**764,628**

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