Business Update
October 2015

Update on Strategy and Financial Projections

Making homes and lives better
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Wheatley Group

The last 18 months has been a momentous period for Wheatley and, of course, Scotland.

Executive Summary

In 2014, Scots had their say on our country's future, while Glasgow hosted the best ever Commonwealth Games. As these momentous events unfolded, Wheatley created its own piece of history.

In November 2014, we successfully issued a £300 million 30-year public bond on the capital markets, the first Scottish housing group to do so. Following the initial £250m issuance at a coupon of 4.375%, the retained £50 million was sold at the UK's lowest – at the time – rate of 3.542% for a housing association public bond.

The confidence shown by investors confirmed Standard & Poor's 2014 AA- rating of Wheatley, which was subsequently upgraded in June 2015 from a stable to positive outlook to reflect the Group's continuing improved financial performance and strong operational management. This £300 million encouraged the Scottish Government to allocate an additional £97.1 million of grant funding to support Wheatley's development programme over the next seven years. Our strong liquidity position – with £236m of undrawn committed bank facilities – further supports this development programme, which will see over 7,400 new homes built by our subsidiaries in the coming years.

Another landmark moment was the addition of the Edinburgh-based Dunedin Canmore Group to Wheatley in June 2015. With overwhelming backing from Dunedin Canmore tenants – 84.3% voting in favour of joining the Group – this highly-respected new partner organisation strengthens our presence in the east of Scotland. We have recently entered into partnership discussions with an Edinburgh-based housing and care specialist, Barony. With a turnover of £7m, this would consolidate the Group's east-to-west strategic footprint in the care market in central Scotland.

Our financial position continues to improve and business performance across the Group remains strong. Our RSLs demonstrated continued improvement across all Scottish Social Housing Charter measures for 2014 – 15, with customer satisfaction remaining over 90% for our largest subsidiary, Glasgow Housing Association, and top quartile performance in key measures such as void levels and arrears. Prudent management and efficiencies saw us outperform our 2014 – 15 budget by £14 million, realising an operating surplus of 17% and a surplus after interest and tax of £9.7 million.

Our financial performance continues to strengthen; we delivered an operating surplus of £32m for the six months to 30 September 2015, with our full year operating margin forecast to grow to 20%. This will be further boosted by an anticipated £97m gain on business combinations from our partnership with Dunedin Canmore.

Our drive to create stronger communities by integrating housing and care services is progressing. Loretto Care's new Tenancy Support Service is now available to our most vulnerable customers, and this has contributed already to a rise in tenancy sustainment. Finally, serving our communities remains at the heart of our work. Almost 700 training, apprenticeship and employment opportunities were created during 2014 – 15 through the Wheatley Pledge, community-benefit clauses in our contracts and our Community Janitor programme.

Who we are and where we operate

Dunedin Canmore joined the Group shortly after the year-end, and therefore is not consolidated in the 2014 – 15 financial results. The completion of partnership with Barony will extend Wheatley's operational footprint to 17 of the 32 local authority areas across central Scotland. The Group's head office is Wheatley House in central Glasgow.

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 Clackmannanshire
17 Inverclyde

The Group's operational entities are:

// Six Registered Social Landlords:

- // *Wheatley Housing Group Ltd – the Group parent does not own any homes, but is registered with the Scottish Housing Regulator and is responsible for providing strategic direction, oversight and business services (such as finance, legal, HR and ICT) to subsidiaries across the Group*
- // *The Glasgow Housing Association Ltd ("GHA") – Scotland's largest Registered Social Landlord, with 39,048 homes in Glasgow (excluding properties classified for demolition)*
- // *Cube Housing Association Ltd ("Cube") – with 3,344 properties across the west of Scotland*
- // *West Lothian Housing Partnership Ltd ("WLHP") – which owns and manages 381 affordable homes in West Lothian*
- // *Loretto Housing Ltd ("LHA") – a specialist provider of supported accommodation with 1,243 properties in west and central Scotland*
- // *Dunedin Canmore Housing Ltd – with 5,879 affordable rented properties across Edinburgh, the Lothians and Fife*

// A charitable care provider, Loretto Care, which supports over 1,000 people with specialist needs, many of whom live in properties owned by its parent entity, Loretto Housing Ltd

// Three commercial entities:

- // *YourPlace (incorporated as Glasgow Housing Association (Management) Ltd) – providing factoring (common property management services) to over 26,000 customers*
- // *Lowther Homes Ltd – with 304 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, as providing property management and repairs and maintenance services to Dunedin Canmore Housing*

Wheatley's position in the Scottish sector

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 rating report from June 2015 noted that:

Wheatley is likely to cement its public policy role and improve its financial profile, through continuing as a key development partner of the Scottish government...

Although Wheatley's business strategy does include significant development, we note that it is still conservative in relation to many English peers, in that its strategy remains focused on developing and operating social housing, with only limited exposure to commercial activities. This should support the predictability of its revenue and expenditure base.

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% of all Scottish housing stock [1], compared to 17% in England [2]. Scotland has a slightly lower rate of owner-occupation than England, just over 60% compared to 65%. The proportion of housing in the private rented sector is 12% in Scotland, compared to 17% in England.

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 opposite.

1 http://www.scotland.gov.uk/Topics/Statistics/Browse/Housing-Regeneration/HSfS/KeyInfoTables 23.8% of housing stock in Scotland is socially rented. Of this 11.1% are rented by Registered Social Landlords and 12.7% by Local Authorities.

2 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/211288/EHS_Headline_Report_2011-2012.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. Applies to tenants in England with income over £40,000 in London and over £30,000 outside London required to "pay to stay".	**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.	Draft 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. Affordable rent support typically limited to <£20,000 per property. S106 planning requirements for social housing being scrapped – reduced pipeline of schemes for social landlords.	New build **grant levels significantly higher than England** (benchmark £62,000 per unit and proposals to increase this) – with ongoing **cross-party support for new affordable housing**, e.g., SNP policy commitment to 50,000 new affordable homes 2016–21 if re-elected
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
Regulatory context	Homes and Communities Agency as regulator, risk-based regulation with proposal for "deep dives" on selected providers.	A different regulator – the Scottish Housing Regulator, which is close to the smaller number of associations and "has demonstrated a **track record of intervening to support failing housing associations**, whether through supervision, mergers, or arranging for additional grant" (S&P, June 2015).
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.

Both Moody's and Standard & Poor's downgraded the outlook on the majority of the English sector during summer 2015. Wheatley is now one of only two UK housing groups on positive outlook from S&P.

Standard & Poor's ratings

Landlord	Rating	Outlook
Notting Hill	AA	negative
L&Q	AA	negative
Sovereign	AA	negative
Richmond HP	AA	negative
Wheatley	AA-	positive
Aster	AA-	positive
BPHA	AA-	stable
Town and Country	AA-	stable
Thrive Homes	AA-	stable
Sanctuary	AA-	stable
Guinness	AA-	stable
EMH	AA-	stable
Cross Keys	AA-	stable
Chelmer	AA-	stable
Boston Mayflower	AA-	stable
Swan	AA-	stable
Colne	AA-	stable
Apex	A+	stable
Home Group	A+	negative

Performance overview

Registered Social Landlords (RSLs)
The 2014 – 15 Annual Returns on the Scottish Social Housing Charter showed that our housing associations either maintained or increased their number of top quartile performance indicators during 2014 – 15. Over half of all GHA and West Lothian Housing Partnership indicators are now in the top quartile in Scottish terms.

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

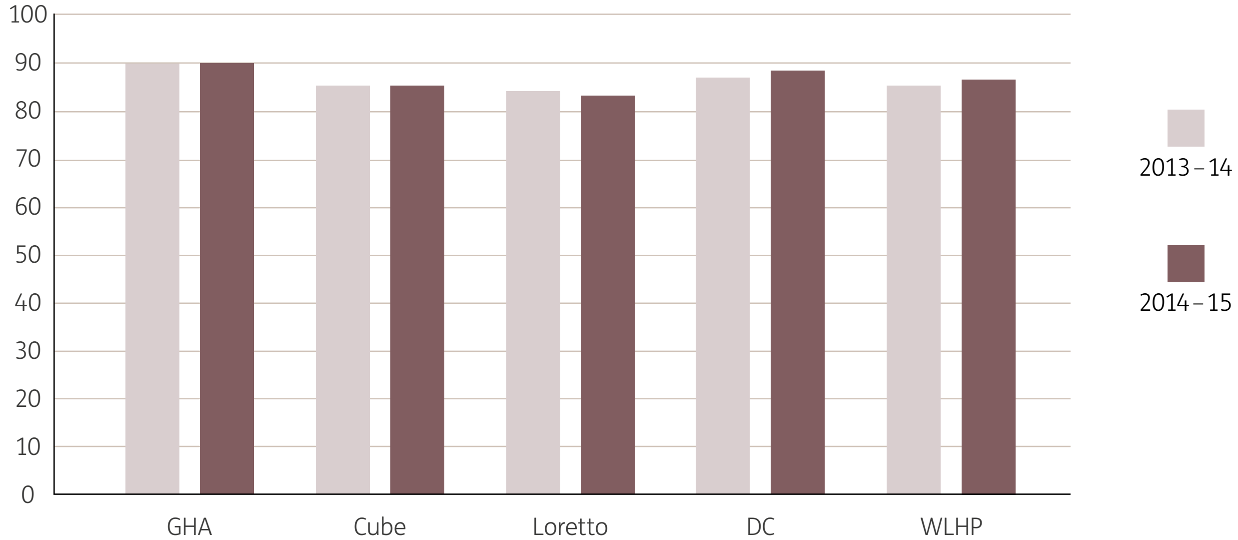
Looking wider, the most recent benchmarking exercise from Housemark shows our largest subsidiary, Glasgow Housing Association (GHA) to be in the top quartile on key measures across its UK peer group. The table below provides an analysis from Housemark against 18 large organisations. The results for the comparator organisations are for 2013 – 14.

Housemark benchmarking results

	Overall Satisfaction	Current Tenant Arrears	Days to Let	Rent Collected	Rent Lost Due to Empty
GHA 2013 – 14	90.64%	2.59%	19.56	99.60%	0.52%
GHA 2014 – 15	90.64%	2.38%	14.39	99.60%	0.33%
Upper Quartile 2013–14	90.34%	3.23%	24.3	96.50%	0.78%
Ranking 2013 – 14	4	2	2	1	1
Ranking 2014 – 15	4	2	2	1	1
No. in Group	14	19	18	19	19

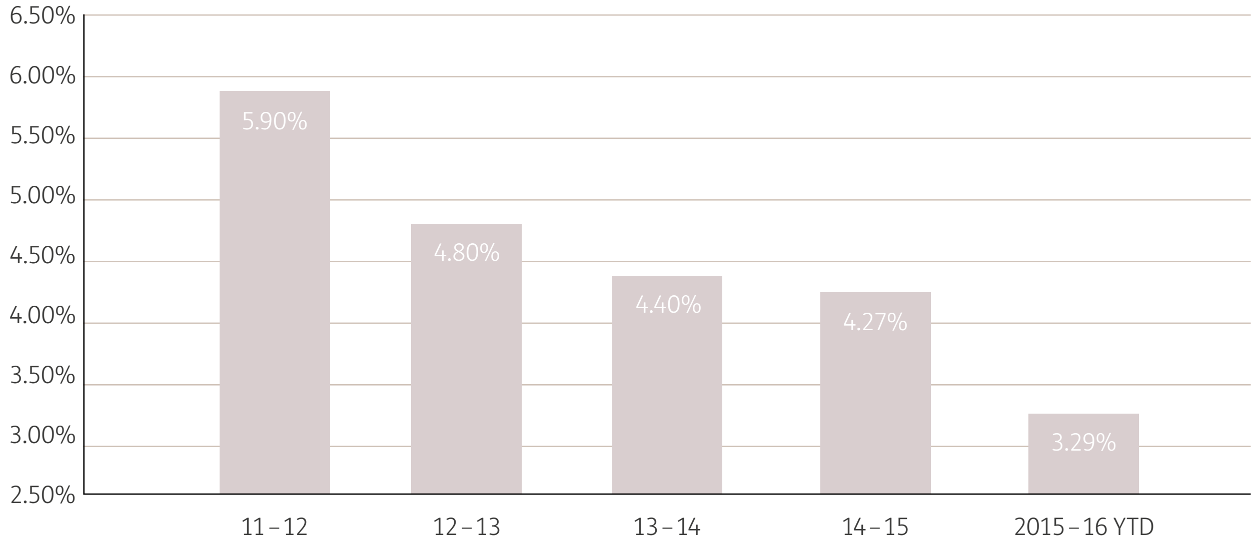
A drive to maintain outstanding customer satisfaction is at the heart of our approach to performance. The chart below illustrates the consistently strong level of satisfaction across all of our housing association subsidiaries.

Consistently outstanding customer satisfaction



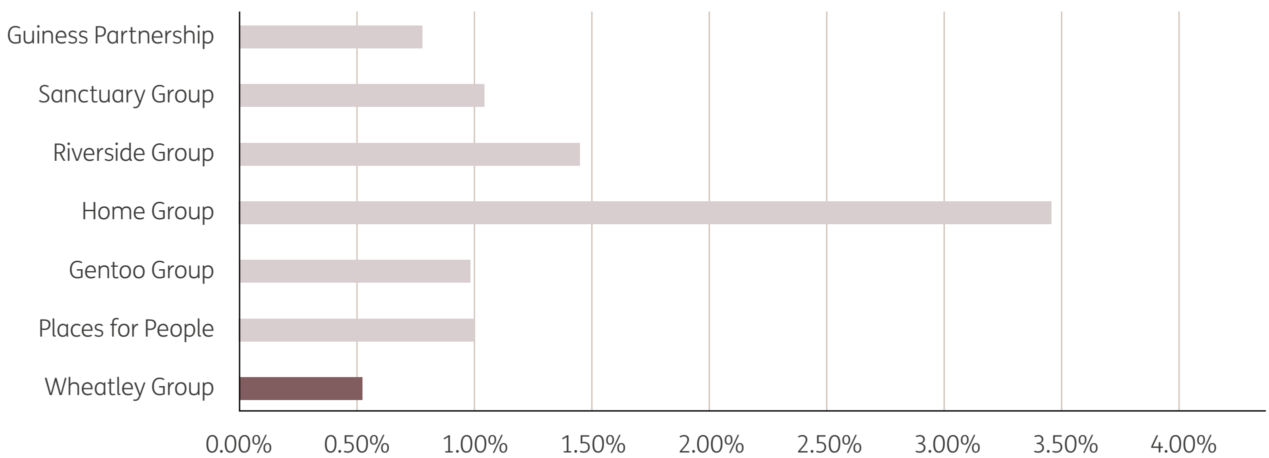
The charts below show positive performance in relation to arrears, voids and days to let vacant properties across the Wheatley Group.

Overall rent arrears (current and former tenants)



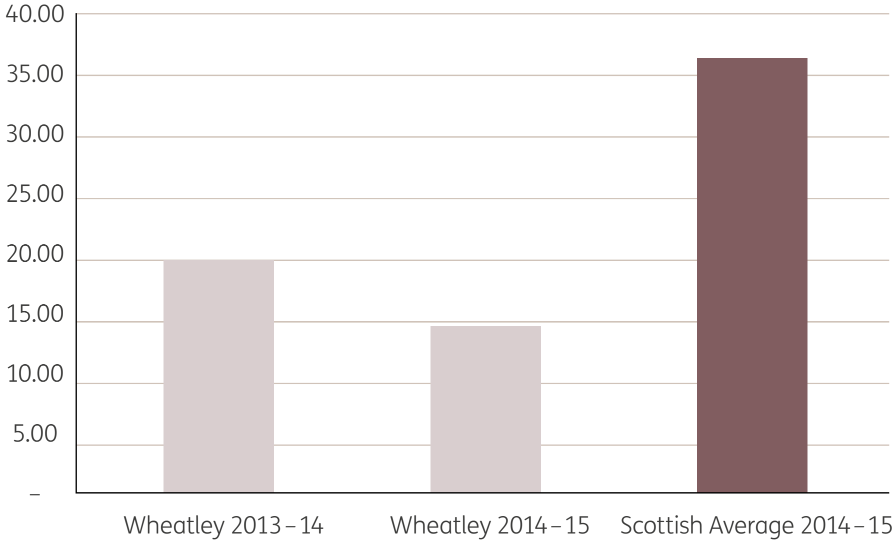
Source: Scottish Social Housing Regulator returns; 2015–16 position as at 30 Sept 2015

Void lost rent vs peers



Source: 2014 – 15 comparator figures from peer annual accounts; Wheatley position reported as at 30 Sept 2015 weighted average of Group RSLs

Average days to let vacant properties



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

Care and support
Loretto's tenancy support service reported strong results, with 88% of customers receiving the service reporting they could now manage their tenancies and 94% saying they could take better care of themselves.

Commercial subsidiaries
For the second consecutive year, YourPlace returned over £0.9 million in Gift Aid to the Group, to be invested back into our communities. The diversification and development of the customer base received a major boost when the company was awarded the contract to factor 700 homes in the Commonwealth Games Village in Dalmarnock, Glasgow.

The excellent business performance of Lowther Homes, which has a growing portfolio of 478 owned and managed properties, ranged from an average of 16.4 days to let a home, against a target of 27, to rent arrears of just 0.78%, against a target of 1%.

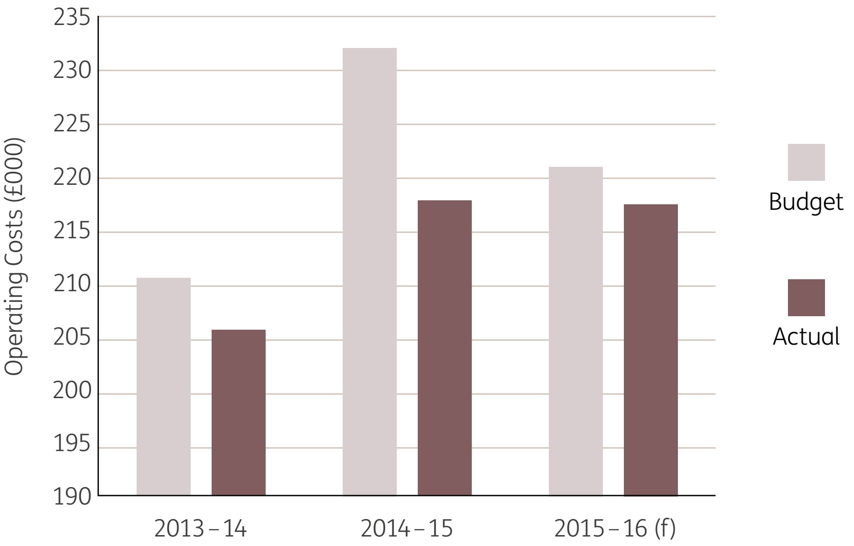
Financial performance
The Group early-adopted FRS 102 and the related Statement of Recommended Practice (SORP) for its 2014 – 15 accounts. The changes move UK accounting practice for non-listed entities in line with International Financial Reporting Standards. For housing providers with listed bonds such as Wheatley, accounting practice is now more closely aligned with other UK entities with listed financial instruments.

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

Statement of Comprehensive Income	**2013–14**	**2014–15**	**2015–16**
	Actual	***Actual***	***Forecast***
	£000	***£000***	***£000***
Turnover	237,106	252,183	270,381
Operating expenditure	(205,235)	(217,553)	(217,625)
Other income and gains	26,770	8,237	96,736
Operating surplus	**58,641**	**42,867**	**149,492**
Operating margin %	**25%**	**17%**	**55%**
Gain on disposal of fixed assets	2,306	2,183	2,110
Net finance costs	(29,867)	(35,270)	(46,150)
Movement in fair value of financial instruments	(48)	2	0
Reversal of previous decrease in valuation of social housing properties	105,054	0	0
Surplus before tax	**136,086**	**9,782**	**105,452**
Taxation	194	(34)	0
Surplus for the year	**136,280**	**9,748**	**105,452**

Note: figures stated on FRS 102 basis for comparison purposes.

Budget outperformance – actual costs v budget



The year to 31 March 2015 saw a strong financial performance across the Wheatley Group. From a turnover of £252.2m (2014: £237.1m), the Group achieved an operating surplus of £42.9m, or an operating margin of 17.0% (2014:£36.8m, 15.5%, before gains on business combinations) and an overall surplus for the year of £9.7m. Total Comprehensive Income for the year of £71.2m (2014: £201.1m) reflected the operating surplus combined with the improving position of the Group's pension schemes. The higher level of Total Comprehensive Income in 2013 – 14 arose from a large revaluation gain on the Group's housing properties that year, following the completion of a significant stage in the Group's investment programme. A continued focus on efficiency and value for money delivered an operating surplus from social lettings of 36%.

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 £11.8m (4.7% of Group turnover) and posted a surplus of £0.3m, while income from investment/commercial property was £5.1m (2.0% of Group turnover).

For the six months to 30 September, turnover was £139.7m, with a full year forecast of £270.4m as Dunedin Canmore's results are consolidated. Operating surplus of £32.1m for the half-year is forecast to grow to £52.8m for the full-year, translating into an operating margin of 20% before gains on business combinations are taken into account. Including the gain on business combinations from Dunedin Canmore, forecast operating margin is 56%.

Even after including none months of Dunedin Canmore results, our Group operating costs for 2015 – 16 are forecast to remain constant at £218m. This is due to compensating efficiencies from workforce planning savings, repair costs falling following our significant capital investments to reach the Scottish Housing Quality Standard by the deadline of 2015, short term initiatives being completed and running cost savings. Some of the last of these have been particularly significant as we deliver efficiency through our enlarged group structure. For example, our reprocurement of insurance on a group basis and rationalisation of offices across subsidiaries has yielded significant recurring savings.

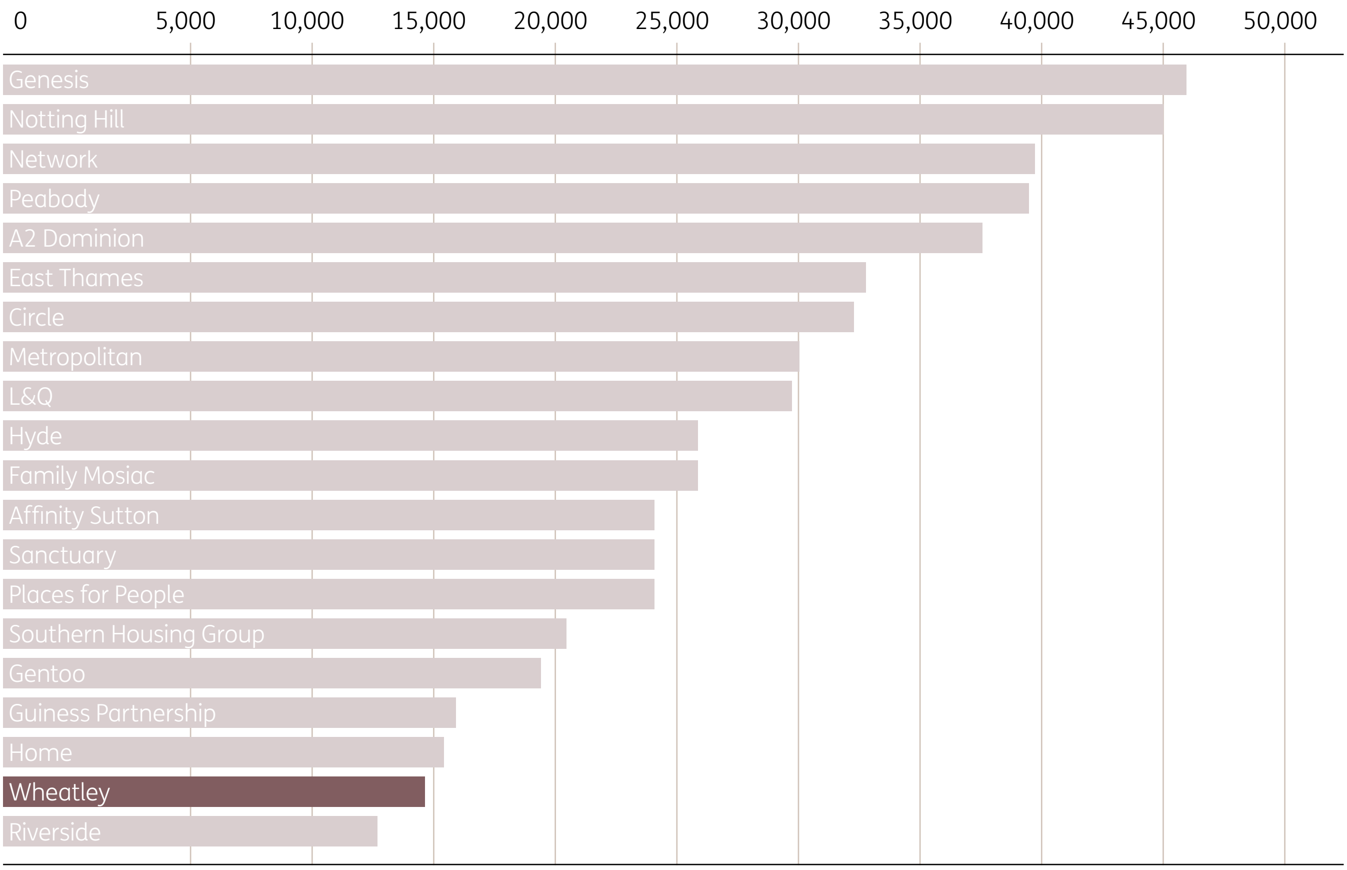
The forecast operating surplus for 2015 – 16 takes into account the gain on business combination with Dunedin Canmore; however even excluding this our margin improves from 17% to a forecast 20% while unit costs are forecast to reduce. We have consistently outperformed our budgeted efficiency targets; the table below highlights overall Group budgetary outperformance over the last three years.

Statement of Financial Position	2013–14	2014–15	2015–16
	Actual	*Actual*	*Forecast*
	£000	*£000*	*£000*
Housing and investment properties	1,153,834	1,241,320	1,632,596
Other fixed assets	22,067	22,644	25,428
	1,175,901	**1,263,964**	**1,658,024**
Pension asset	0	10,684	10,684
Trade and other debtors	169,003	146,144	128,744
Cash and cash equivalents	30,904	101,996	**33,560**
	199,907	**248,140**	**162,304**
Creditors <1 year	(91,493)	(97,312)	(104,755)
Net current assets	**108,414**	**150,828**	57,549
Creditors > 1 year	(618,211)	(762,878)	(988,520)
Pension liability	(57,484)	(7,831)	(15,255)
Provisions for other liabilities	(142,296)	(117,262)	(79,525)
Net assets	**466,324**	**537,505**	**642,957**
Revenue reserves	392,189	466,322	571,774
Revaluation reserve	74,135	71,183	71,183
Total reserves	**466,324**	**537,505**	**642,957**

The Group Statement of Financial Position at 31 March 2015 showed an increase in the value of housing properties during the year of £87.5m (8%), reflecting the on-going benefit of the investment we make in customers' homes and our new build programme. Capital and reserves have grown by 15% to £537.5m, 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 £731.0m (2014: £587.5m) 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 51%. Net debt per unit was £14,000 (gross debt excluding cash in hand was £16,000), below the majority of large UK housing groups.

Net debt per unit comparisons



Source: 2014 – 15 annual accounts

At 30 September 2015, net assets had grown further to £650.9m with the acquisition of Dunedin Canmore. The Financial Golden Rules – reviewed annually by our Group Board and set out below – were also comfortably met at 30 September;

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 cove red 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 £20,000 across RSL borrower group
Interest Cover	Adjusted operating surplus (adding back depreciation and RTB gain on sales) to be greater than or equal to 1.1x across RSL borrower group
Operating Margin	RSL and commercial entities to both move towards a minimum operating margin of 20%

Cash flow and liquidity
The Group Cash Flow Statement for 2014 – 15 demonstrated a strengthening operating cash flow. Net cash inflow from operating activities was up by 15% to £45.4m (2014: £39.4m).

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 £37.6m was drawn down during the year (2014: £40.7m). Cash of £102.0m was held at 31 March 2015, reflecting the retained bond issuance in January 2015 as well as early receipt of £14.5m of new build grant from the Scottish Government and actual expenditure for 2014 – 15 being £14.0m (6%) below budget for the year.

Strong liquidity and low refinancing risk
As part of the bond issuance process, the bank funding of GHA, Cube, West Lothian Housing Partnership and Loretto Housing was restructured. The individual bank loans held by each RSL (some of which were held under syndicated arrangements) were rolled over and consolidated into a new Group treasury vehicle, Wheatley Funding No.1 Limited (WFL1) at Group level. Each of these RSLs now has the ability to borrow from a Group funding facility through an intra-group loan agreement with WFL1, secured by assets from the RSL Group.

At the same time a £50m real estate finance facility was also put in place for Lowther Homes Limited, funded through Wheatley Funding No.2 Limited (WFL2), the new treasury vehicle for our non-charitable subsidiaries. This

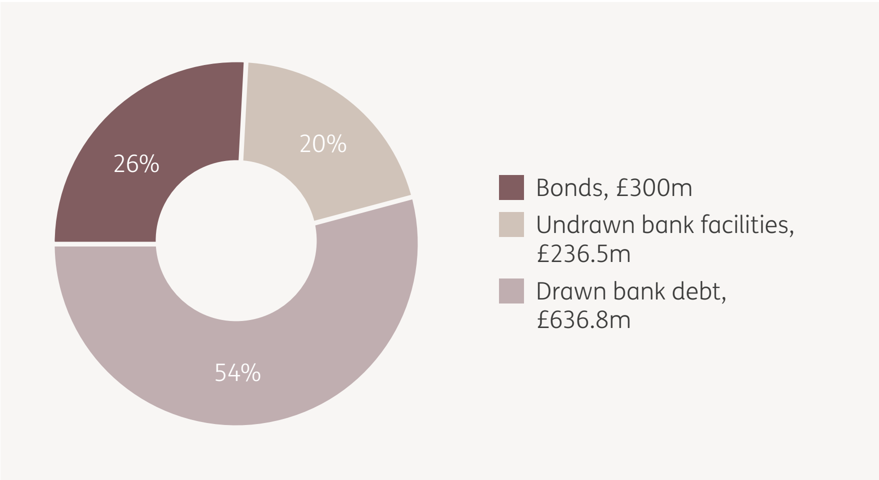
was secured on Lowther Homes assets with the previous senior secured on-lending facility from GHA converted into an unsecured subordinated loan. At the year end this £50m bank facility remained undrawn.

When Dunedin Canmore joined the Group at the end of June 2015, they brought their existing funding into the Group, consisting of £138.5m of syndicated commercial bank facilities, £16.5m loan from The Housing Finance Corporation and £9.8m commercial loan for Dunedin Canmore Enterprise (through WFL2).

At 30 September 2015, the Group therefore had £1,173.3m of bond and bank funding facilities in place, with WFL1 funding facilities secured on assets of certain Group RSLs, WFL2 facility secured by assets of Lowther Homes Limited and Dunedin Canmore Enterprise and Dunedin Canmore Housing loans secured by their assets. The funding facilities in place on 30 September 2015 comprised the following:

Group Co	Facility	Principal
WFL1	Bond – maturity Nov 2044	£300.0m
	Commercial bank syndicated facility	£526.0m
	European Investment Bank facility	£132.5m
DCH	Commercial banks syndicated facilities	£155.0m
WFL2	Private rented sector bank finance	£59.8m
		£1,173.3m

Twenty per cent (£236.5m) of the Group's borrowing facilities were undrawn at 30 September 2015.



The weighted average duration of drawn debt across the Group is 21.9 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 only re-financing risk in year six relates to £50m of bank loan facilities for the Group's commercial subsidiary, Lowther Homes, based on typical market terms for commercial debt. The historic weighted average cost of drawn debt, inclusive of margins and hedging activities, was 4.98% at 31 March 2015 on an annual effective rate basis (2014: 4.48%).

The principal cash outflows during 2014 – 15 were operating costs and investment in assets, particularly in development of new housing stock of £71.9m (2014: £25.2m) and investment in existing stock of £51.8m (2014: £72.9m).

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