**APPENDIX 2**

# Bushloe Developments Ltd

# Business Plan

# May 2017

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## 1. The Purpose of the Company

1.1 Oadby and Wigston Borough Council has a desire to build homes in its own right but is precluded from doing so due to borrowing constraints.

1.2 The Council currently has around 500 families on its housing register and there has been a 50% increase in homelessness in the last year.

1.3 By forming a local housing company it will assist the Council in addressing the demand for affordable homes, reduce homelessness and also to provide a valuable source of income for the Council.

1.4 The primary purpose of the company will be to deliver new homes but will also have the ability to engage in other commercial activities. Properties will be let at both affordable and market rents subject to demand.

1.5 The secondary purpose of the company will be to carry out business development activities, to research new ways and opportunities by which it could support the achievement of the council's wider objectives. Some ancillary expenditure towards this purpose is anticipated in the initial business plan period. The company will then present proposals, in the form of a revised business plan, for approval by the council, ideally before the end of the 2017/18 financial year.

## 2. The benefits of operating as a company

2.1 As a wholly owned, Local Authority Company, the company will operate at 'arms length' from OWBC, with the remit of providing affordable/market rented accommodation to households for which OWBC has a responsibility.

2.2 The company would be set up with the following requirements:

- After the initial set up period, the company operates with a retained surplus The company will have discretion over the individual properties it acquires or develops
- They are in a suitable location within Oadby and Wigston.
- That 30 % of the homes will be affordable.

## 3. The structure of the company

3.1 The company will be set up as a company limited by shares, initially providing affordable and market rent homes.

3.2 The company will be named Bushloe Developments ltd.

3.3 The company's registered office will be:

Bushloe House
Station Road
Wigston
Leicestershire
LE18 2DR

3.4 The Company's Memorandum of Association and Shareholders Agreement are as set out in the relevant documents.

3.5 The Board of the Company will be chaired by an Independent Director Stephen Glazebrook. The other directors of the company will be:

- Anne Court Director of Services OWBC
- Chris Raymakers Finance Manager OWBC

3.6 In terms of Governance there will be an advisory Board consisting of:

- Leader of the Council and 2 Elected members
- The Chief Executive and the Section 151 Officer of OWBC

3.7 The company may purchase some services under a Service Level Agreement with OWBC including

Support Services Property
Services

3.8 The Company may purchase such other services as may be required to discharge this business plan under contract procured to demonstrate value for money including but not limited to:

Property management and routine maintenance Major
maintenance and refurbishment
Rent collection and debt recovery
Buildings Insurance
White Goods
Professional services for business development activities, to the extent that these are affordable and consistent with the governance framework.

## 4. The Company Financial Plan

### 4.1 Property Portfolio

4.1.1 The intention is that Bushloe Developments will seek to build new homes, purchase existing properties for sale on the open market and acquire gifted properties as a part of Section 106 Agreements and to manage the new proposed homeless hostel at Belmont House, Station Road ,Wigston

4.1.2 The plan for the acquisition of properties (say 20) would commence during 2017/18 and will continue until the end of the 2018/19 and possibly beyond subject to finance being available

4.1.3 For the company to be financial secure it is important that the right mix of properties be developed and acquired.

4.1.4 In terms of the acquisition of existing properties the intention is that a broad portfolio of properties will be purchased within specific areas:

- Oadby ( average house price £212K)
- Wigston ( average house price £ £177K)
- South Wigston ( average House price £163K)

4.1.5 To be a sustainable viable company a minimum excess of income from rental above operational costs will be required. In developing or purchasing a property, this margin can be expressed as a Gross Margin as a percentage of the rental compared to the final purchase price.

## 4.2 Capital Investment

### 4.2.1 Capital Expenditure

4.2.1.1 Modelling the development costs of 2 identified sites and the acquisition of 20 properties during the first 2 years suggests a Capital requirement of about £10 million (depending upon the average gross yield achieved and the mix of properties acquired.

4.2.1.2 For a given indicative pool of properties, the capital requirement reduces as the Gross Margin increases.

4.2.1.3 The funding model is based on a 'bullet payment'. The company services interest on the debt only, the debt (and equity) being repaid upon the liquidation of the asset.

### 4.2.2 Funding of capital investment

4.2.2.1 The capital investment can be funded from a mixture of loan and equity capital. The amount that the company can afford to borrow will be determined by the availability of revenue funding to meet the interest payments on any borrowing. The amount of revenue funding available to meet repayments on capital will be driven by the Gross Margin.

4.2.2.2 As the Gross Margin increases, the amount of income generated from rents increases in proportion to the amount borrowed. Any capital that the company cannot raise through borrowing could be made available from OWBC in the form of Equity in the company.

Equity would be an investment in the company whereby the financial return on the investment would take to form of dividends (annual share of any profits) or on liquidating the company's assets at some time in the future. If (say) the Authority lent the company 95% of its capital requirement and made the rest available as equity, a 1% p.a. rise in the value of the property would represent a 20% p.a. growth in the value of the equity held in the company (before tax).

## 4.3 Company Operational Finance

### 4.3.1 Company Turnover

4.3.1.1 Based on a final investment portfolio of up to £ 10m and a Gross Margin of 5%, the estimated turnover of the company would be £110K in the first year of operation, rising to £646K in year 3 once the development programme has been completed and the properties let to tenants.

### 4.3.2 Operational Expenses

4.3.2.1 The company will operate with minimal operational expenses. There will be a core company cost including the salary costs of the managing director. Other costs include property management, finance and legal, and directors expenses (LHC).In addition there will be costs associated with re-letting properties, minor and major maintenance, voids and bad debts. Allowance for all of these costs has been included in the financial modelling.

### 4.3.3 Company Tax Status

4.3.3.1 As a limited company registered under UK company law, the company will be liable to pay UK taxation on:

- VAT on inputs into the company – charges from the Local Authority and contracts for maintenance and management of the portfolio of properties. The company would not be able to offset VAT as the value of taxable supplies will be very small
- Corporation Tax – a taxation of the profits made by a company
- Capital Gains Tax – a tax upon the rise in the financial value of an asset

4.3.3.2 In addition, the company would be liable to pay Stamp Duty Land Tax on purchases for the property portfolio.

### 4.3.4 Financial performance

4.3.4.1 The company's financial performance is dependent upon a number of variables:

- The profile of the properties within the portfolio
- The timing of the development and purchase of the properties
- The Interest rate charged on any borrowing

- The costs of refurbishing prior to first let
- The length of time between purchase and first occupancy Annual running costs and rental income

4.3.4.2 Based on these assumptions the financial model suggests that an overall loan to equity split of 95% loan, 5% equity maintains the right balance between benefits to the local authority and the viability of the company.

4.3.4.3 Modelling using the parameters outlined earlier in the business plan and the assumption contained within appendix 1, the company is forecast to begin operating at a profit from year 2 onwards.

4.3.4.4

| **5 yr Summary Forecast Trading Statement** | **Year** | | | | | |
|---|---|---|---|---|---|---|
| | **0** | **1** | **2** | **3** | **4** | **5** |
| | | £'000's | £'000's | £'000's | £'000's | £'000's |
| Gross Rental Income | 0 | 110 | 379 | 646 | 1,062 | 1,478 |
| Management / Maintenance and Bad Debts / Voids etc. | | (22) | (76) | (130) | (212) | (281) |
| LHC Costs | (10) | (100) | (100) | (100) | (100) | (100) |
| **Net Operating Income** | (10) | (12) | 203 | 416 | 750 | 1,097 |
| | | | | | | |
| Debt Financing | | (70) | (140) | (210) | (360) | (360) |
| Working Capital | 10 | 82 | 0 | 0 | 0 | 0 |
| | | | | | | |
| **Net Operating Profit / (Loss)** | 0 | 0 | 63 | 206 | 390 | 737 |
| | | | | | | |
| Corporation Tax | 0 | 0 | 13 | 41 | 78 | 147 |
| | | | | | | |
| Retained Profit | 0 | 0 | (50) | (165) | (312) | (590) |
| | | | | | | |
| Retained Profit (Cumulative) | 0 | 0 | (50) | (215) | (527) | (1,117) |

### 4.3.5 Cash Flow

4.3.5.1 A 24 month Cash Flow forecast indicates that the company will need a working capital facility of £100,000 until year 2, at which point it begins to accumulate retained surpluses. Interest on any working capital facility has been calculated at the same rate as the overall capital interest rate charged on the borrowing element of the development/property purchases.

## 5. Sensitivity Analysis, risks, Issues and mitigations

### 5.1 Sensitivity Analysis

5.1.1 Operating at LHA rental income, the company operational financial margins are small. For that reason it is proposed that the company will offer a mixture of affordable and market rent tenancies. Therefore the company needs to be sensitive to a number of factors that underpin its performance. The key Factors being:

Gross Margin Inflation
Management of voids and bad debts
Property portfolio

5.2 Risks, Issues and Mitigations

5.2.1 There are a number of financial risks facing the company. The sensitivity analysis shows that the biggest risk is at the acquisition/development stage. It is critical to the sustainability of the company that the right mix of properties is acquired for the portfolio.

5.2.2 Analysis of risks, issues and mitigations

| **Risk / Issue** | **Impact** | **Mitigation** |
|---|---|---|
| Portfolio of properties does not achieve the target Gross Margin<br><br>The portfolio of properties can sustain the company for the early years, but is not able to sustain for the full 30 year plan | The relative income from property rentals at LHA rates is insufficient to fund the full business plan of the Company<br>The company becomes insolvent | Property acquisition is targeted to achieve the target gross margin.<br><br>Properties could be transferred to a different rent model with a higher yield than LHA rents. |
| LHA income inflation does not achieve the increases in the model | The company cannot achieve the required income levels | Properties could be transferred to a different model of social rent with a higher yield than LHA rents |
| Cost Inflation is higher than included in the model | The company's cost base is higher than that included in the model | Properties could be transferred to a different rent model with a higher yield than LHA rents |
| Contract management / re-let and maintenance costs are higher than modelled | The company's cost base is higher than that included in the model | Properties could be transferred to a different rent model with a higher yield than LHA rents |

## 6. Key Targets

6.1.

| Key Target | Measure | Impact | Verification |
|---|---|---|---|
| Gross Margin | Greater than 4% for affordable housing and Greater than | A minimum gross margin is required in order to make the company sustainable and a higher margin is expected from | |

| | | | |
|---|---|---|---|
| | 5% for Market rents | commercial investments | Based on detailed financial analysis underpinning the company business plan |
| Borrowing | 95% | A 0.2% increase in the Gross margin will increase the income available to the business by £ 60K over the 30 year business plan | |
| Equity | 5% | Higher revenue costs or below target gross margin will | |
| Cash Flow | Peak working capital requirement | The company requires a working capital (cash flow) facility during the initial business plan period whilst properties are developed/ purchased, refurbished and first let | |

6.2. These key targets are dependent upon a number of key variables that underpin the finance model in the company business case

| | | | |
|---|---|---|---|
| Tax | Corporation tax, VAT, Stamp Duty and Land Tax | | The model informs the potential for payment of Tax |
| Turnover | 4 year average tenancy turnover | A higher turnover of properties would increase the number of families housed but would potentially increase void maintenance costs and potentially rent loss | The average turnover has been modelled based on experience. |
| Housing Management and Maintenance Service | 10% | A higher cost would reduce the share income available for loan repayment. A lower cost would increase the stability of the company and support an increased loan to equity ratio borrowing ratio or provide funds for additional investment | The rate per property has been based upon market knowledge |
| Insurance | £200 per property p.a | A cost at variance to this would have an impact on the financial model | This is based upon experience. The final property portfolio will drive the insurance costs. Internet research suggests that the average cost of buildings insurance in the consumer market is £84 p.a. |
| Voids and | 1.5% void | A higher cost would reduce | The expectation is |

| | | | |
|---|---|---|---|
| Bad debt | 2% bad debt | the share of income available for loan repayment. A lower cost would increase the stability of the company and support an increased loan to equity ratio borrowing ratio or provide funds for additional investment | that the client group would be likely to be able to meet rent obligations. |
| Major works | 0.5% of property value per annum after 4 years | A 1% increase/decrease in the Major Works costs would result in an increase or decrease of the business plan of plan period | The actual cost of major works will be tested during the life of the business case. The cost of works will be flexed depending upon the condition of the property at point of re-let. |