

AFFORDABLE HOMES STRONG COMMUNITIES



THEMATIC REVIEW

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# Disposals

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April 2007

# Introduction

In 2006, the Housing Corporation introduced Thematic Reviews as a new regulatory product. These reports use existing sources of data that we hold on housing associations and examine performance by specific sections of the housing association sector.

Thematic Reviews are designed to comment on important issues facing the sector and are one of a number of ways that the Corporation provides valuable feedback to both housing associations and their key stakeholders. They enable our regulators to come to an overview of sector performance and identify outliers, and may be used to influence proportionate and targeted regulatory engagement.

They also enable associations to use the analysis to benchmark their own performance against their peers. In *How We Regulate 4: Our Overall Approach* we outlined that the Corporation's corporate priorities and emerging risks will determine the topics that we select for Thematic Reviews.

This report is one of the four Thematic Reviews that the Housing Corporation has undertaken during 2006-07 and focuses on the level of disposals by housing associations. It follows a steady rise in the surplus reported on sales and the

concern expressed by some of the sector's stakeholders that associations are 'selling the family silver'.

To understand what has been going on within the sector a small team from within the Corporation has been looking at four years' worth of regulatory and statistical return (RSR) and annual accounts data, as well as the most recent set of FV5 financial forecasts to understand the changing dynamics of housing associations' disposal strategies and to see where the sector may be heading. This has been supplemented by qualitative analysis and case studies to try and get behind the numbers and understand the business drivers behind the changes.

The report begins by looking at the different types of disposals made by the sector and at the characteristics of the disposing associations. It then maps these disposals to the financial performance of associations to see if there is any correlation between the two and builds on the analysis carried out in the 2005 Global Accounts about the dependence of associations on sales proceeds to make a surplus.

This analysis leads to a discussion of the growing importance of shared ownership developments for the sector's finances

and the different risk profile to which this exposes associations. The report concludes with some thoughts on the new risks that the sector is being exposed to and how the Housing Corporation can identify and help associations to mitigate them.

# Executive summary

- The recent high-profile cases of associations selling rented units to fund major repairs programmes are relatively isolated cases;
- There is little correlation between associations with tight financial positions and those selling rented units outside the sector;
- There has been a marked increase in the number of associations involved in shared ownership and a corresponding increase in the number of units being built;
- Shared ownership is no longer a specialist activity and the surpluses generated by shared ownership sales have become an integral part of many associations' business plans;
- Associations are more exposed to the housing market than ever before, helping them enjoy substantial gains from the growth in house prices, but they need to ensure they understand the risks they are taking on, including the impact of a potential downturn in the market;
- Overall the sector could probably cope with a 10-20% drop in house prices, but this would severely impact on their ability to deliver new units.

# Housing association disposals

## Basis of analysis

In order to assess the level of disposal activity and its impact on the sector recently, we have used two main data sources: the RSR (in particular section K on sales, transfers and demolition) and the FVA return, which captures the statutory accounts of associations. The key area of interest here has been the surplus that associations return on disposals.

The RSR asks for information on a number of different types of disposals and over a period the definitions have varied slightly, so in order to simplify our analysis and to enable comparison over time, the different RSR categories have been grouped into four key types:

### Sales to existing tenants

Including right to buy (RTB) and right to acquire (RTA) sales where the association has an obligation to dispose of its property to a sitting tenant if requested.

### Shared ownership sales

Where associations have built units explicitly for shared ownership purposes and therefore it does not count as a disposal of a rented unit.

### Sales within the sector

Disposal of stock (sometimes tenanted) to other social landlords. As such this does not represent a net loss to the sector.

### Sales outside the sector

Occasions where associations dispose of stock to purchasers other than tenants or other social landlords.

By using this four-category approach we are able to quickly identify the types of disposal that are taking place and to understand some of the drivers behind associations' disposal strategies.

## Levels and type of disposal

Graph 1 shows the levels of disposals that have taken place between 2002 and 2005 across the different categories.

The graph shows that the single largest category of disposals was the sale of properties to existing tenants. In most years this was followed by shared ownership sales and then disposals to other landlords (both social and non-social).

This is an important corrective to the view sometimes given that associations sell significant amounts of stock to organisations and private individuals outside the sector.

Indeed, sales outside the sector never amount to more than 15% of the property sold in any given year.

Over the last three years of the analysis (2002-05) the volume of units being disposed of has stayed reasonably constant – approximately 26,000 to 30,000. This is in contrast to the surpluses being made on disposal which have grown in the same period by 53%, suggesting that associations have benefited from a very buoyant housing market. This is explored further below.

It should be noted that in 2004-05 we have adjusted for approximately 2,500 units that were disposed of by associations in

Graph 1: Disposals by type



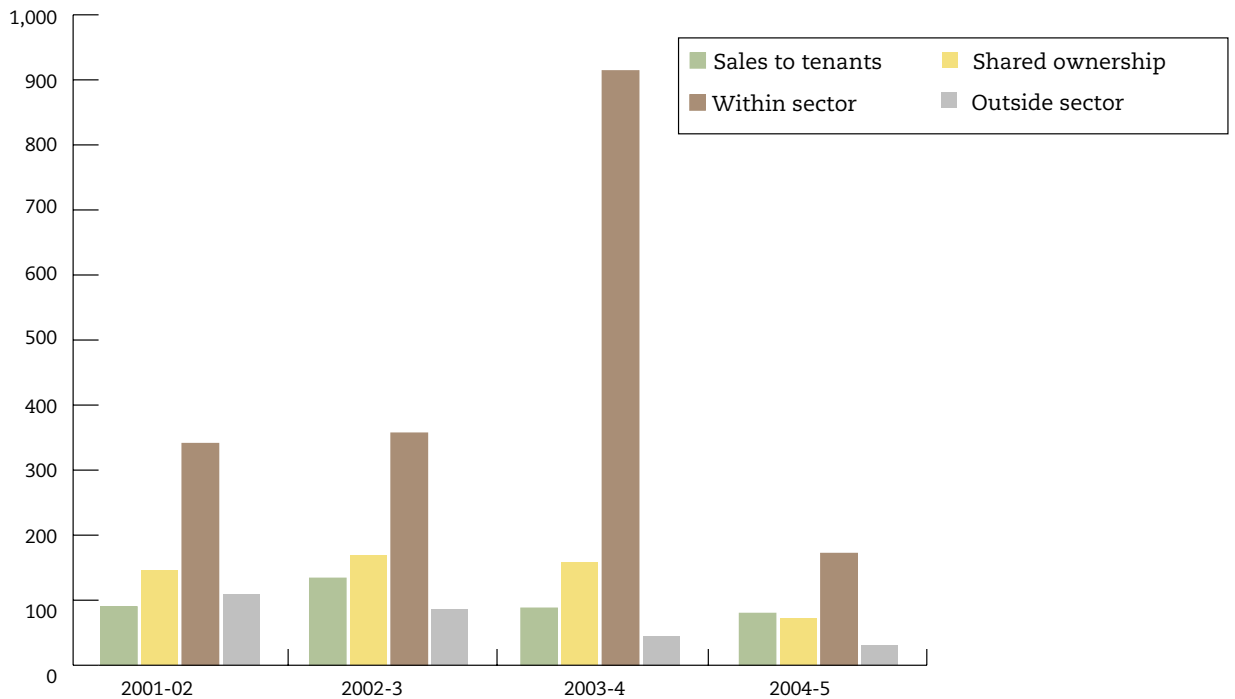
pathfinder areas. On the RSR form these were disclosed as out of sector sales, but these were a combination of disposal for demolition/remodelling and tenure diversification that were part of wider area regeneration strategies.

As such it was not thought appropriate to treat these as typical disposals of rental stock. However, even including these units in the analysis, the 2004-05 disposal levels are below those for 2003-04. In short, there has not been a significant increase in disposal volumes of late.

## Volume of disposals per association

Graph 2 shows the average number of units sold per disposing association for the four main disposal types. It shows that there is a significant disparity between the profile of disposals to social landlords and other types of disposal. The former are categorised by a small number of large disposals, whereas the latter are made up of a larger number of smaller-scale transactions.

Graph 2: Volumes of disposals by type



It is also interesting that there is no particular trend in the volume of disposals per association for any of the categories except shared ownership, which has increased every year albeit only marginally. Disposals outside the sector actually fell between 2003-04 and 2004-05.

This lack of a trend suggests that disposals other than shared ownership disposals are not becoming an integral part of associations' business planning. The sales to tenants are largely driven by the actions of those tenants, whilst the disposal of stock to other social landlords often reflects the movement of stock within groups, or as part of a development partnership, rather than a need to generate cash for the business.

The disposals outside of the sector also vary from year to year, casting doubt on suggestions that associations are progressively selling units to prop up underlying business plans. However, this proposition is explored in more detail below.

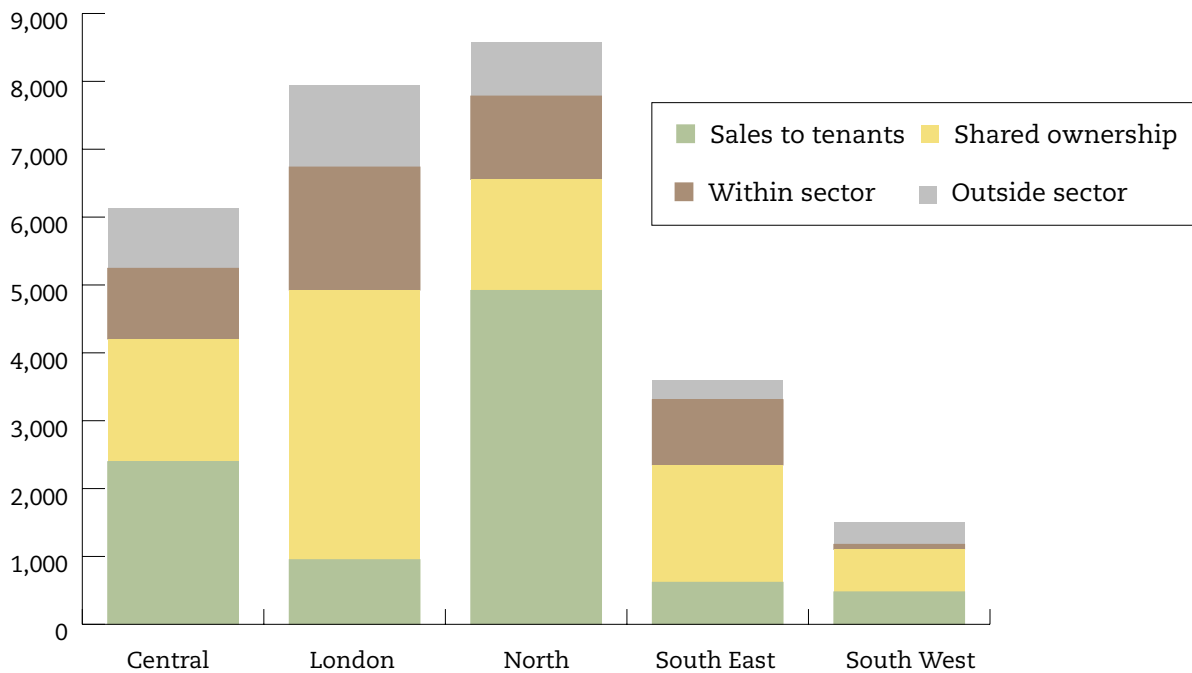
## Geographic differences in disposals

The picture is even more interesting when a geographic filter is laid over the data. Graph 3 shows an analysis of the 2005 RSR disposals by the geographic location of the association.

The instructive comparison here is between London associations and those regulated in the North. The London associations' sales are clearly dominated by disposals to shared ownership residents, as to a lesser extent are the sales in the South West and South East. In contrast the sales made by the Northern associations are heavily weighted towards the sale of rental units to existing tenants, with significantly fewer shared ownership sales being recorded. Interestingly, the Central region represents a mid-point between the North-South split.

This clearly shows us that at a macro level there are key environmental drivers behind disposal strategies. In areas where the market has been buoyant for a prolonged period, shared ownership is clearly an attractive development proposition for associations. However areas that have seen a great deal of recent stock transfer activity are dominated by the disposal of stock

Graph 3: Disposals by region



to tenants, as they take advantage of the relatively affordable price of their improved properties. Although Graph 3 represents a one-year snapshot, the picture holds true for all of the years covered in this survey and the results for the previous years are shown in Appendix 1.

There is, however, an important caveat to the information shown in Graph 3. The geographic location is taken as the place where the association is regulated from and not from where the stock has been disposed.

Although there remains a strong correlation between where associations are regulated from and where they hold their stock it is not exact, and some associations hold stock nationally yet have their figures reported in just one region. Despite this the results shown in Graph 3 do tell an interesting story about the geographic dimensions of stock disposal.

## Disposals and surpluses

As shown in the preceding sections, the volume of disposals has not increased significantly over the past three years, however it is clear from the Global Accounts published by the Housing Corporation that the sector has become increasingly dependent on property sales to enable it to report a surplus each year. Graph 4 shows how the level of surplus reported in the Global Accounts has developed over the four-year time frame.

What is noticeable is that, unlike the figures for the volume of disposals, there is a clear trend in the amount of surpluses being reported – it is rising steeply. Indeed between 2001-02 and 2004-05 the surplus on disposal rose by 132%, suggesting that associations have enjoyed a significant cash injection as a result of rising house prices.

This rise in profits on disposals, combined with a small number of high profile cases – mainly in London – has led some of the sector’s stakeholders to wonder whether associations are effectively ‘selling the family silver’ in order to finance existing commitments, and in particular to meet the Decent Homes Standard and to cope with constrained rent levels. On the face of it

this case would appear to be supported by the Global Accounts, as for the past three years the sector would not have shown a surplus before tax if it had not delivered significant profits on disposal. However, as discussed below, the balance of evidence is that the rise in profits on disposal is because of their changing composition rather than an increase in the volume of ‘out-of-sector’ sales.

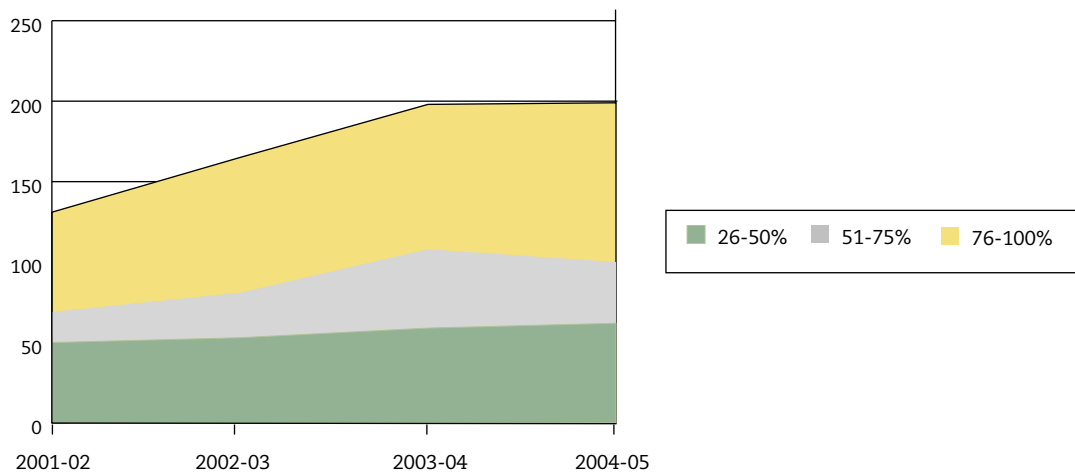
What is true at a macro level is also true at the micro level; increasing numbers of associations are dependent on sales to report a surplus. The overall sector position is shown in Graph 5. The number of associations being at least 25% dependent on disposals for their surplus has risen steadily, but it is the cohort of associations that are at least 75% dependent on sales proceeds that has shown the most significant increase.

The main concern for the sector’s stakeholders is that this increased surplus is being driven by the sale of existing rental units onto the open market, suggesting that associations are depleting their asset base to meet short-term viability targets. Given that over the same period as the rise in profits on disposal the fact that the volume of sales outside of the sector has not been showing a steady increase – but

Graph 4: Surplus on disposal



Graph 5: Surplus dependence of housing associations



instead has been fluctuating year-on-year – suggests that at a macro level the sector is not meeting gaps in business plans by

selling off existing units. However, this does not mean that there are not individual associations which are taking this path,

and in order to look at this in more detail, the RSR information on disposals has been correlated with the FVA data on surpluses on disposals, and this is discussed in the next section.

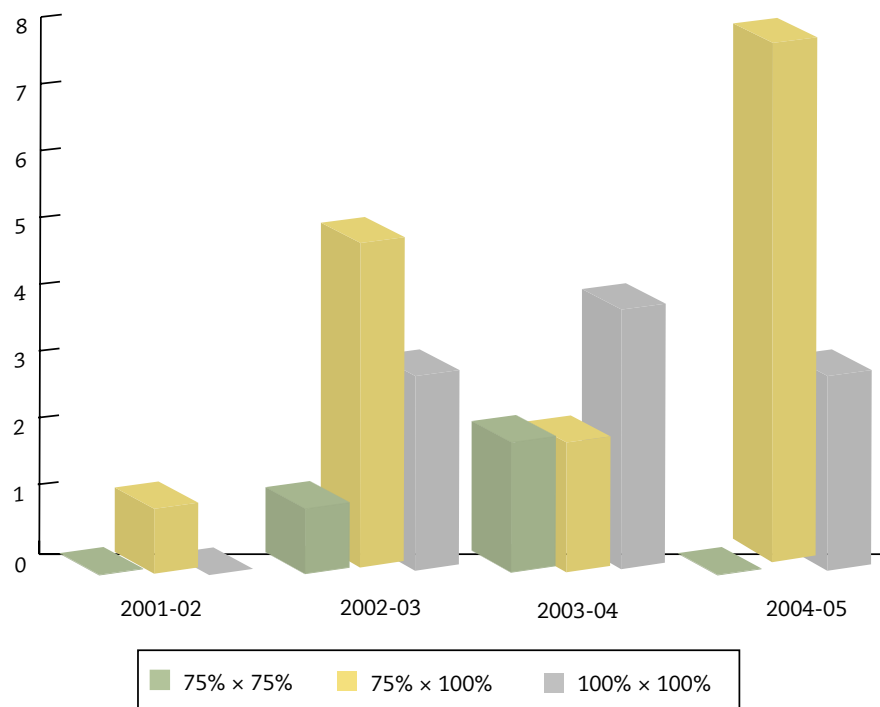
### The relationship between disposals and surpluses

As explained above, associations have little control over the number of tenants who exercise their right to buy or acquire their homes; shared ownership units are built

to be sold; and the disposal of properties between social landlords normally represents inter-group transactions or development agreements. This means that the only control associations have over raising cash through the sale of rental units is if they are disposed of on the open market, i.e. they are sold outside of the social housing sector.

The review of the data has already shown that at a macro level there is little evidence

Graph 6: Correlation of non-social housing sales and sales dependence



to show a trend of more units being sold voluntarily, however the data was also interrogated to look at those associations that were generating at least 75% of their surplus before tax through sales, and where at least 75% of the units being sold were outside the sector. The results are shown in Graph 6.

The graph shows the number of associations in each year where each risk factor is at least 75%.

Even at this level of analysis it is clear there is very little correlation between sales outside the sector and those associations dependent on disposals to generate a surplus. Even in 2004-05 there were only 11 associations with at least a 75% by 75% correlation, representing just less than 2% of the total population of 556 lead regulated associations.

In order to understand what caused these associations to be in this position, our field teams reviewed the data and our existing knowledge about these associations. The results are instructive. In all cases the associations were disposing of units identified as part of an asset management strategy of which the Corporation was aware. In the majority of cases the

associations involved were stock transfers that were making very small surpluses because of the unique way such businesses are financed, and generally the volume of units being disposed of was small, i.e. less than 15 per association per annum. The only significant exception to this was a very small number of mainly London-based associations. In these cases the units were being disposed of as part of an asset management strategy but they were not stock transfers and the volumes were higher than 15 units.

In other words, despite the recent press coverage, there is little evidence that associations are selling off their asset base to fund their ongoing activities. There have however, been a small number of high profile cases that have distorted the view of some of the sector's stakeholders.

What is undeniable is that the sector has seen increases in the level of surpluses from property sales and that this trend has been ongoing for some time. Understanding what is driving this trend – and therefore what the risks might be if this benign trend does not continue – is dealt with in the next section of this report.

## Shared ownership sales and surplus generation

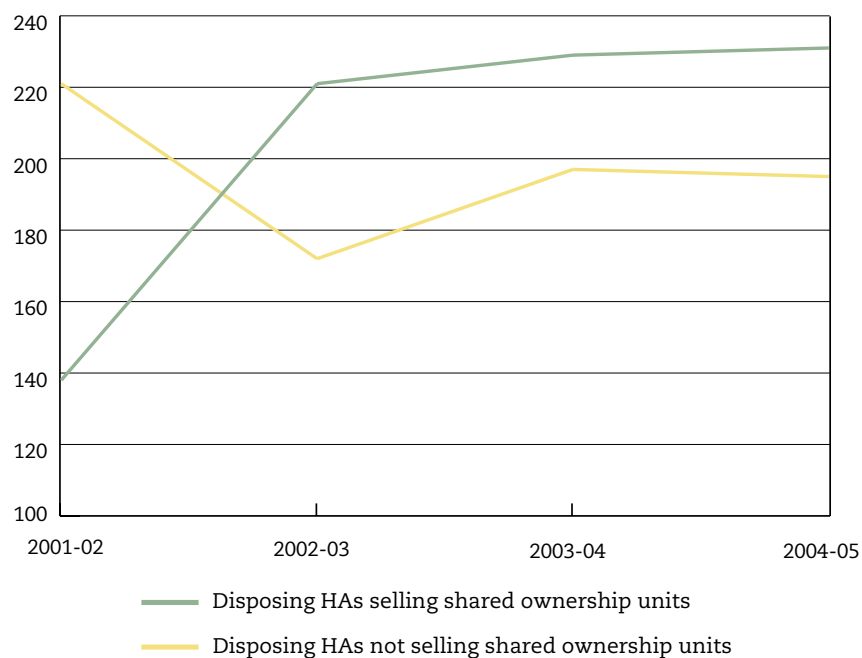
Over the course of the four years under review, an important shift took place in the nature of social housing disposals.

In 2001-02 the majority (62%) of the associations which reported sales activities in their accounts didn't report any shared ownership disposals, whereas by 2004-05 this situation had reversed and the majority of disposing associations reported shared ownership sales (54%).

As Graph 7 shows, in absolute terms the picture is even clearer. The number of associations which reported disposal activity, but no shared ownership disposals fell slightly over the period. However the number of associations which reported shared ownership activity increased markedly in the same period.

In the past, shared ownership sales were seen as the preserve of a small number of specialist associations, but now more and more organisations are becoming involved. Indeed, the figures for 2004-05 suggest that

**Graph 7: Prevalence of shared ownership sales**



almost half of all associations over 250 units were involved in some kind of shared ownership disposal.

This fits in with the 2006-08 allocation round where 240 individual associations received funding for developing shared ownership units. It also emphasises how shared ownership is becoming a useful way of delivering a diversity of tenure within new developments and is helping the Government deliver its policy of an affordable route into home ownership.

However, the spread of associations carrying out shared ownership is heavily weighted to the southern half of the country and to London and the South East in particular as shown in Graph 3. This point is reinforced in Table 1, which shows, by region, the

percentage of disposals that were shared ownership sales for each of the four years.

For all regions except North and Central, shared ownership was the largest type of disposal made, and for all regions it was the largest category of sales apart from the sale of property to sitting tenants via RTB and RTA. It was also the category that grew in importance in all regions over the four years.

This reinforces the view that we are seeing a structural shift in the nature of associations' businesses, particularly where there has been a buoyant housing market and demand remains high. It seems likely that it is the shift to shared ownership that explains why the surpluses on disposals have risen so sharply even though the volume of disposals has remained relatively static.

**Table 1: Percentage of shared ownership sales by region**

	2001-02	2002-03	2003-04	2004-05
London	50%	53%	58%	50%
South East	36%	36%	58%	48%
South West	14%	31%	32%	42%
Central	16%	27%	23%	29%
North	12%	24%	14%	15%

It also suggests that shared ownership units are significantly more profitable than other forms of disposal. Over the four years of the study period surpluses on disposal rose by 132% compared to a rise in general house prices in England of 70%<sup>1</sup>. Although the calculation of disposal proceeds is not directly analogous with house prices, the fact that profits have increased at twice the rate of house price inflation does suggest that the structure of the housing association property disposal market has changed. In particular, there appears to have been a shift from price-capped RTB-type sales to a form of sale that enables an association to gain more exposure to the upside of the general housing market.

This mainstreaming of shared ownership has important implications for the sector as such activity carries a very different set of risks and rewards from the traditional rental activity carried out by associations. In order for the sector and its regulator to understand this changing risk profile, the remainder of this report looks at the forecast information the Corporation has received from associations to assess their potential exposure to the vagaries of the housing market and what impact this could have on the delivery of affordable housing in England.

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<sup>1</sup> Communities and Local Government, English House Prices Index, Table 506

# Housing association forecasts

## The risks and rewards of shared ownership

Before looking at what associations are forecasting over the next five years, it is worth looking at why associations have shifted to shared ownership and how the risk and reward profile differs from traditional rental activity.

With rented units, associations finance the construction costs through a combination of grant, debt and internally-generated cash and then they use the net cash flow from the rental income to pay off the debt over the long term, typically 20 to 30 years. With shared ownership units, the three sources of funding for the construction costs are supplemented by the sale of a proportion of the value of the asset to the homeowner, this is typically between 25 and 50% of the asset's value and is referred to as the first tranche sale proceeds.

The association charges a rent on the remaining unsold equity in the property which is used to finance the outstanding debt. The homeowner then has the option to increase the percentage of the property they own (referred to as staircasing sales) as their financial position allows. These subsequent tranches are sold at their prevailing

market value, rather than the value of the property when it was first sold. This enables associations to benefit from rising property values and to book larger profits if the market continues to rise. If property prices fall then associations are likely to find themselves having to sell subsequent tranches at a loss, because the capital value of the property has fallen, making it cheaper for the owner to staircase upwards. However, if asset prices are falling then it is likely that owners will put off buying further tranches for fear that there will be further falls in value. In this scenario, the volume of sales could dry up and any sales made could be at a considerable loss to the association.

Throughout most of its operation housing associations have only known a rising market and in the last ten years annual house price inflation has been running in double digits. In effect developing shared ownership units has become a 'one way bet', where associations are often able to generate significant surpluses from the development of these units. This has come at a particularly helpful time for associations, particularly in London and the South East, where the impact of rent restructuring and rent caps has meant that the development of rental units has become less profitable, and on many schemes

associations have needed the surpluses generated from shared ownership units to cross-subsidise the rental developments and to enable the associations to pay back their debt in a reasonable timeframe.

This has had the effect of making many associations' finances dependent on shared ownership sales if they wish to carry on developing. This is something that many of the sector's stakeholders have come to recognise over the last few years, including lenders who are increasingly allowing associations to bring the surplus from sales into their interest cover covenants. It is also a trend that the Housing Corporation has observed over the last few years through our Annual Viability Review (AVR) process and which we have commented on in our Field Financial Reviews. The London review in particular has observed that many developing associations are only able to meet their interest obligations through shared ownership sales.

This scenario is not in itself worrying, unless associations fail to continue to sell shared ownership units at both the price and volume necessary to sustain their financial position. Given the high demand for affordable housing in London and the South East, where most of the shared

ownership units are built, such a situation seems unlikely, but, as the recent experience in the United States shows, it is by no means impossible. Moreover, an increasing number of economic forecasters are suggesting that in the near term we can expect a downward 'correction' in house prices of between 10 and 20%. Given all the changes that have taken place in the sector since the last property slump in the early 1990s we do not know how the sector would deal with falling house prices, but what we do know is that the sector has greatly increased its exposure to the sale market, as opposed to the rented market, and this poses significant challenges for associations.

## The impact of falling house prices

To look at the impact of reductions in either the price or the volume of disposals the Corporation carried out a range of sensitivity analyses on the same data set of associations as used in the recent Unlocking the Door publication. These 347 individual associations and groups form 75% of the total sector by number of units and can be taken as a strong representative sample. The data used was supplied to the Corporation via FV5s and Capacity Models and as such represents associations' own data, in a high-level format.

The approach taken was to flex the assumptions so that changes were made to both the price achieved for units and the volume of units sold. To measure the impact on the business we looked at the underlying

cash flow. Because of the high level of the data all units were flexed as it is not possible on the FV5 form to differentiate between the types of units being sold (RTB, shared ownership etc), however, if there was to be a drop in house prices then it would apply to all types of property and not impact only on shared ownership units, for example. The final important caveat is that the impact of loss-making associations, including early years stock transfers, has been included as although their business plans anticipate making losses they are often dependent on RTB sales and any fall in house prices would impact on them.

The flexes that were carried out were to adjust for different falls in house prices (down 5%, 10% and 15%) and for reductions in the volume of sales (down 10%, 20% and 30%). The results for this are summarised in Table 2.

**Table 2: Impact of scenarios on free cash flow**

All figures in £m	2005-06	2006-07	2007-08	2008-09	2009-10	Total reduction
Base	-470	-233	84	294	450	N/A
Price -5%	-549	-334	-17	190	347	-489
Price -10%	-625	-431	-113	94	253	-947
Price -15%	-703	-530	-211	-6	154	-1,421
Volume -10%	-513	-283	20	223	369	-311
Volume -20%	-557	-334	-44	151	288	-622
Volume -30%	-600	-384	-108	79	206	-932

The table shows the free cash flow available to associations after they have met all of their operating costs (including capitalised costs) and their existing interest payments (including capitalised interest). Because of the inclusion of the loss-making stock transfers, the baseline position shows a net cash outflow for the first two years. However, even allowing for this, the message from the flexing is clear: a reduction in sales price and/or volumes would severely impact the financial capacity of the sector, with reductions in sales prices of 15% removing £1.4 billion of expected cash from associations' business plans.

It is also clear from the flexing that associations are more susceptible to actual price reductions, rather than simply selling properties at a slower rate. Whilst neither situation would be beneficial for associations, a 10% drop in prices would be three times more serious than a 10% drop in the volume of sales. Clearly a combination of the two would be far more serious and is also highly possible if there is a general market slowdown.

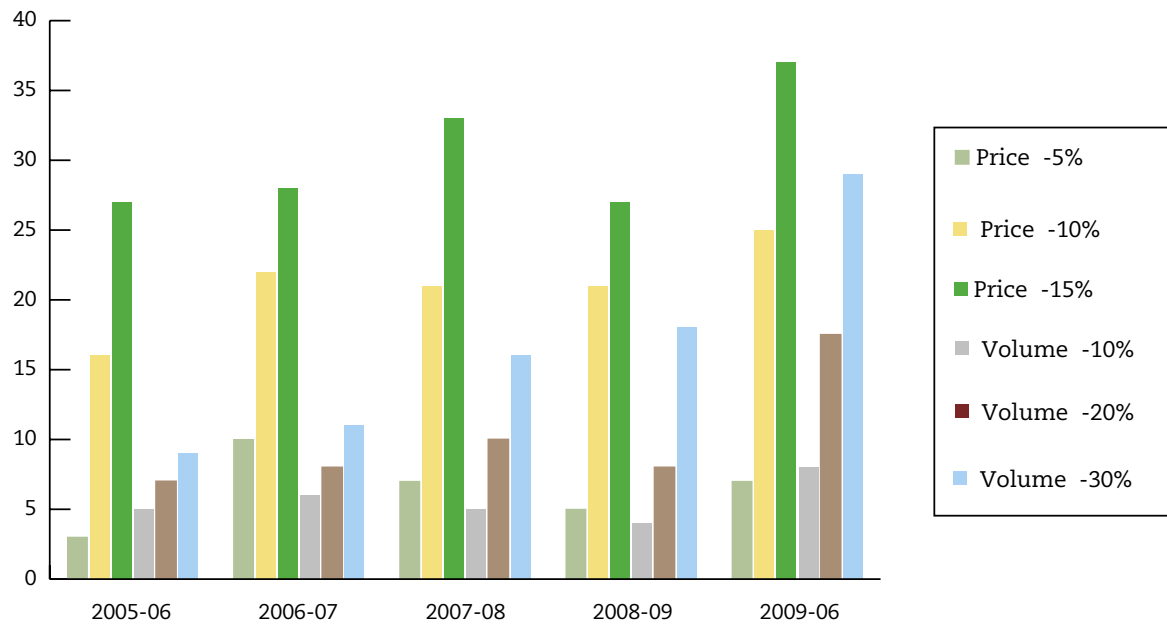
In order to get a sense of how many individual associations would be affected by these scenarios, the number of organisations that would move from having a positive free-cash position in the base case to having a negative

position (i.e. those that would not generate sufficient cash from operations and sales to meet their interest payments) was mapped and the results are shown in Graph 8.

The most encouraging thing is that the numbers involved would be relatively small. Even in the worst case the figure is 37, just over 10% of the sector. Given that in macro terms the sector would have seen its cash flow reduced by up to 70%, such a low rate is reassuring. What this hides is that many associations already have a negative cash flow (mainly stock transfer associations, but including some traditional ones). Associations in this position amounted to between 25% and 30% of the sample population. It is likely that the position for these associations will have deteriorated significantly and will constrain their ability to deliver on their business plans.

It should be noted that all the business plans being flexed are assuming a certain level of development as well as disposals. If the cash being generated by disposals was to fall then associations would look again at their planned levels of development, and would also consider other options for protecting their financial position. As a result a significant fall in house prices is unlikely to result in associations going out of business,

Graph 8: Impact of flexes



but would probably result in a reduced supply of new housing.

### Lower house prices and development capacity

Even if, with a drop in house prices of 15%, some 60% of the sector would still generate enough cash to pay its interest costs and deliver the units in its business plans. There are still serious implications for the ability of the sector to deliver on the agenda set out by the Housing Corporation in *Unlocking the Door*. In that publication it was estimated

that the same data set as used in this survey would have the theoretical capacity to raise an additional £6.9 billion if associations used sales proceeds to help meet interest payments to finance additional debt. In that publication we recognised that associations each have different priorities with regard to investment in new and existing stock and that they also will have different risk appetites making it unlikely that all associations would wish to take on this full theoretical additional debt. This report helps to inform that debate further by showing that the reductions in cash flow shown by

the flexing in this report indicate that for each 5% drop in sales prices that capacity is reduced by approximately £1.3 billion and each 10% drop in volume of sales would see the capacity reduced by around £0.5 billion. Moreover, as discussed above, a drop in house prices that impacts on associations' viability would see them pull back on discretionary activity, including new house building, and this would severely constrain the delivery of new units unless it was politically possible to increase the grant rate. The great unknown in our modelling is what would happen in the wider macro-economic environment in a period of falling house prices, reduced interest rates, increased government intervention in the housing market etc. All of these factors could change the way associations behave and the impact of falling prices on their business plans. At the same time, associations affected adversely by changing conditions in the housing market would take action to protect themselves from those changes where possible.

In this sense disposals and disposal policies at associations have become intrinsically linked with the development of new units. In essence this has three main drivers:

- the funding structure of shared ownership has allowed this product to cross-subsidise rented units for associations. This has come at the same time as the opportunities for shared ownership have increased because of S106 agreements, in addition to the traditional SHG-funded route;
- the Decent Homes Standard and issues of low demand have encouraged associations to look more critically at their asset base. This has meant investing more in existing stock where appropriate and disposing of units that are no longer needed; and
- the significant number of new stock transfers entering the sector over the last ten years has dramatically increased the level of RTB disposals and these have become integral to the funding of transfer business plans.

The net effect of these changes is that associations are having to link their asset management strategies with their development aspirations and their long-term funding plans. In the light of these developments the Corporation is consulting on a revised HCA investment traffic light that will assess how well associations are bringing all these issues together to deliver for new and existing tenants, and for communities.

## Key risks for associations and how to spot them

It is clearly not possible for associations to avoid the risks of the housing market if they want to deliver shared ownership units, but what are the key risks they face, how can they spot them and how can they be mitigated?

At the highest level the risks for associations are simply that either they will not be able to sell enough units or they will not be able to sell them at the right price – which is why we carried out the flexing above – but there are several reasons why they may find themselves in this situation. This could be down to external factors such as:

- interest rate rises;
- market conditions;
- employment rates; and
- inflation levels.

Or it could be down to internal issues including:

- poor customer service;
- misjudging local demand;
- poor marketing; and
- cost over-runs on construction.

As a regulator our concern is that these risks could reach such an extent that an association's viability would be threatened if the organisation was not able to take action to mitigate the risks. In an era of risk-based regulation it is clearly inappropriate for us to second guess associations on how they research local demand, market their properties or deal with customers. However, as shared ownership becomes a mainstream activity for associations and as they come to rely on it for their financial strength and development capacity, so the robustness of the assumptions used in this area become a key concern for us. There are a number of ways we will look at this, including the assessment of the fourth traffic light and the analysis of the Capacity Models submitted by significant development partners.

One of the areas we will look at will be the assumptions made on shared ownership activity, including both the number of sales expected compared to their historical average, the cost of building those units and the expected sale price for those units. In our experience the associations that run into trouble with shared ownership are either those who significantly increase their activity or who are overly optimistic in their assumptions. In the past it has not been uncommon to see business plans where

sales prices are expected to grow at nearly 10% per annum whereas build costs increase at only RPI+1%. Whilst this may not have been an unreasonable assumption in the late 1990s, it is unlikely to be appropriate over the next ten years.

We will therefore be looking closely at associations who are increasing their shared ownership exposure or who are significantly dependent on the cash generated by these sales to fund the rest of their programme. We will want to know how robust their assumptions are and we will use the full range of flexing and Monte Carlo analysis afforded by the Capacity Model to look at what happens if the natural optimism bias is stripped out of the plans. We do not wish to stop associations becoming involved in this area, but given its increased importance to the sector and the potential volatility of the income stream, we will want to understand the assumptions used and challenge associations where we feel they are being overly optimistic.

It is also true to say that we will look at all association asset sales where we believe the organisation is becoming dependent on them to fund their business plan, especially where they are asking us to fund new development. Our approach will be similar

to that applied to shared ownership, looking at the underlying assumptions, testing how deliverable they are and analysing what is driving them. Where appropriate we will also flex these assumptions to test their robustness.

## Conclusions

This Thematic Review has looked at the available data on housing association disposals primarily from a financial perspective. This has helped to demonstrate that, in general, associations have not been disposing of units outside the sector to fund holes in their business plan. It is however true that the profits generated from sales have increased markedly in the last five years, although this seems largely to have been driven by an increase in the proportion of shared ownership units. Finally we have tested the assumptions used by associations going forward, this has revealed that although association viability is unlikely to be threatened by a downturn in the housing market it could seriously impact on the sector's ability to deliver new units.

With this in mind we have tried to set out in general terms how we will approach the assessment of shared ownership assumptions when assessing bids to the 2008-10 National Affordable Housing Programme and how we will seek to ensure associations are sufficiently mitigating their risks in this area.

# Appendix

## Sales by region



## Breakdown of 2003 data by region



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