

AFFORDABLE HOMES STRONG COMMUNITIES



THEMATIC REVIEW

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# Efficiency

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May 2007

# Introduction

This is one of the four Thematic Reviews that the Housing Corporation has undertaken during 2006-07. These 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.

This review provides an analysis of the Annual Efficiency Statements (AES) submitted to the Corporation in 2006. The AES reporting process provides the means by which associations self-assess their performance on improving efficiency. The process was developed in response to the publication in March 2005 of the requirements for both local authorities and housing associations to deliver and report on efficiency gains set out in Sir Peter Gershon's report and the Government's Spending Review 2004 (SR2004) the previous year.

Circular 03/05 sets out our requirements on associations to provide – in the AES – analysis of the three procurement work streams defined by Communities and Local Government (CLG): capital works; management and maintenance; and commodities, and to assess their performance looking back at the previous year's out-turn against targets on a self-

assessment basis (the backward look) and then set targets for the coming year (the forward look). In addition to the three work streams, we invite associations to provide details of any other efficiency gains achieved or forecast.

As part of our analysis of the first year returns, we published a sector study by HQN Limited providing an overview of AES 2005 returns, and commissioned a number of efficiency briefings by the Chartered Institute of Housing. The sector study reported a high rate of compliance with the return requirement, and the forecast performance on efficiency gains significantly exceeded the targets for 2005-06 for the sector as a whole, and for each of the work streams.

This review is an examination of the second year of AESs submitted in 2006, providing the backward look of actual gains achieved in 2005-06 and forward look forecasts for 2007-08. It focuses on the delivery of forecast targets, and provides assurance to government that the sector is delivering efficiency objectives on the ground, as well as on paper, and that it will continue to meet targets in future years. The analysis was carried out by analysts based in each of the Corporation's field offices. It looks at

the sector's performance on a segmented basis to see if trends can be identified and combines AES data with other sources of data captured by the Corporation that helps us form a judgement on both high and low performing outliers in relation to efficiency.

The publication includes an analysis of the numbers provided in AESs. It is split into four sections:

- Analysis of the actual efficiency results recorded in the backward look for 2005-06.
- Analysis of how the actual results compared to the forecasts provided in 2005.
- Analysis of efficiencies forecast for 2007-08.
- Analysis of other information we set alongside the AES.

The Appendix provides case study examples of AES commentaries provided by associations that provide some insight into how efficiencies are achieved and how standards are maintained.

# Executive summary

The sector reported substantial efficiency gains in 2005-06 and, in the majority, provided information within AES returns that demonstrated the significance associations place on improving the efficiency and effectiveness of service delivery.

The 2005-06 gains reported by associations reflect savings well ahead of CLG's interim targets set for the year. The actual recorded savings of £81 million for capital works, £130 million for management and maintenance and £27 million for commodities exceed the respective targets of £2 million, £35 million and £10 million by a total of £191 million.

In addition to the work stream savings, associations reported other whole organisation savings of £80 million. Approximately £27 million of these are attributed to improvements in treasury management activities through refinancing and renegotiation of debt portfolios.

Efficiency gains recorded in 2005-06, represent 3.5% and 4.0% respectively of the aggregate turnover and total expenditure of the sector in the year to March 2006.

The average (per unit) savings delivered through the three work streams for all associations is £121. When the other (non work stream) savings are included, the average per unit efficiency gain is £162.

Although performance varied considerably between associations, actual gains achieved in 2005-06 are very close to the total forecast in 2005. Overall, the outturn varied from the forecast by just £7 million, or 2.2%. The largest variance is reported in the capital works stream, which achieved efficiency gains of 17% less than forecast. This was due in the main to changes in the inflationary indices allowed for comparison and changes in planned programmes of works.

The forecasts for gains in 2006-07 exceed the interim targets set by CLG for the year. In 2005 the sector forecast gains in 2005-06 of over four times the target set; in 2006, the sector forecast gains for the 2006-07 year of double the target.

Although capital works and management and maintenance forecasts for 2006-07 are significantly above the relevant interim targets (£134 million combined), the forecast for commodities is equal to the target, at £30 million. In looking forward to 2007-08 and the final year of the SR 2004 targets, associations have some way to go to achieve the final target for commodities of £55 million. A number of associations did not incorporate savings recurring in actual efficiencies achieved and forecasts for 2006-07. The gains forecast for some associations are therefore understated, although the sector totals as a whole will not be materially affected. We will revise the template and guidance we provide for AES returns to clarify that recurring savings should be reported to ensure we have full information.

The fourth work stream – for new supply efficiencies – measures gains achieved in the application of social housing grant and is calculated and reported by the Corporation directly. This review excludes the analysis work related to this work stream for which the target for increased efficiency by March 2008 is £160 million, with an interim target for 2005-06 of £130 million. However results for 2005-06 indicate the sector is well on the

way to delivering the new supply savings, achieving actual efficiency gains of £392 million.

In summary, the sector is well placed to meet CLG's targets for efficiency gains of £355 million a year by 2007-08. This total comprises: capital works (£60 million), management and maintenance (£80 million) and commodities (£55 million), to be reported through the Annual Efficiency Statement process and new supply target reported by the Corporation.

# Analysis of efficiency gains in 2005-06

We received a total of 371 AES returns from those association groups and individual associations which met our submission requirements<sup>1</sup>. In order to help associations provide the information required in AESs we issued a standard pro-forma AES return on our website in April 2006 and encouraged associations to use this. We undertook checks on the returns to ascertain whether the information provided was reasonable and whether it accorded with other information we have on associations. The result of the sense checks led us to exclude some outlier results from the analyses and findings from the sense checks are referred to within the analysis.

The pro-forma enables a standard presentation of the required analysis by work stream of efficiency gains made in the year to 2005-06 and that forecast for 2006-07. In addition to the requirement to provide the analysis we invite associations to provide commentary on six areas, to demonstrate how efficiencies are achieved and how standards are maintained.

The six questions were:

- What is your value for money (VFM) strategy?
- What activities are you undertaking to secure your efficiency gains?
- How are you involving your residents?
- How is efficiency monitored in your organisation?
- What measures are in place to ensure that service standards are maintained?
- Where are any gains to be reinvested?

Commentary on these areas and examples of good practice are identified in the Appendix, but at a broad level, we rated each category on the quality of the commentary provided.

The majority of returns were completed using the pro-forma, although the extent of its use varied slightly across the country. Analysis was demonstrably easier when the pro-forma was used and helped in our interpretation and analysis of the financial information. We presented a revised pro-forma in April 2007 for the AES statement due in July 2007 and encourage associations to use this.

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<sup>1</sup> Circular 03/05: Annual Efficiency Statements is available from [www.housingcorp.gov.uk](http://www.housingcorp.gov.uk). All associations owning more than 250 units of accommodation were asked to submit an AES at group or individual association level.

Each of the six areas was rated on the quality of the content. Thirty-three per cent were considered comprehensive and considered, 52% satisfactory and 15% contained only very basic details (Table 1). The judgement was based on the extent to which associations demonstrated commitment to improving efficiency by use of examples, providing additional financial information incorporating key association specific targets and indicators. Those returns assessed as comprehensive and considered tended to provide evidence supporting their assessment, for example identifying key local initiatives and setting out the results of performance monitoring.

Those returns that provided in the main only the financial figures for each work stream with limited commentary and little or no evidence supporting their comments were assessed as basic.

**Table 1: Summary of the quality of returns**

33%	Comprehensive and considered return
52%	Satisfactory return
15%	Basic return

In order to provide analyses of the data to understand if there are trends in savings recorded by differing associations, we have analysed the efficiencies based on the regulation field of association (this tends to be the Housing Corporation field where the associations group parent is based), the type of association (whether stock transfer or not) and the comparative size of associations. Table 2 highlights the nature of associations providing the returns.

There has been a significant amount of activity in group structural changes and transfer of engagements which means that some associations reported for different entities in the backward looks and forward looks. In general these were dealt with sensibly – where separate financial records remained for the year 2005-06, usually individual backward look returns were completed. For the forward look, usually a combined AES was produced, with forecasts for the new group entity. Where the AES was produced on a basis different to last year's this was usually referred to, although a small number of returns did not make clear to which associations the group return related.

Table 2: Attributes of associations providing returns

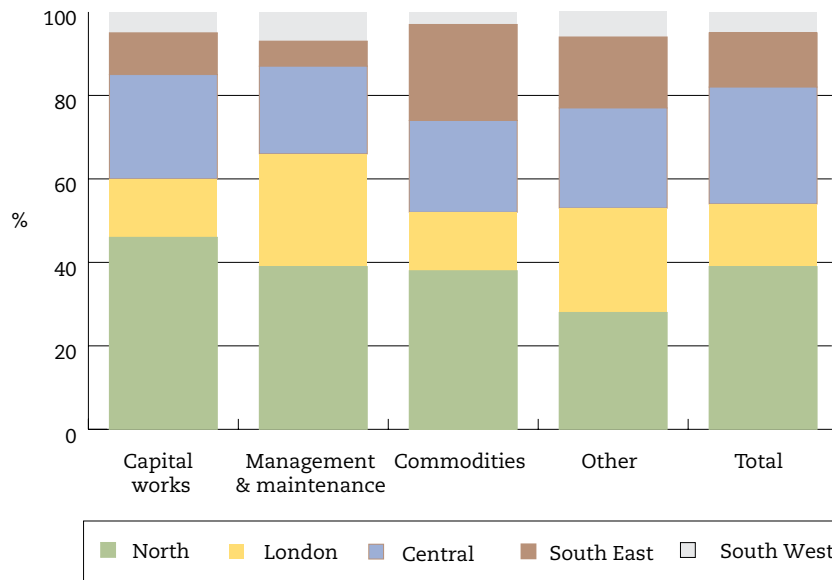
	Central	London	North	South East	South West	Total
Returns per field	103	78	96	55	39	371
Returns based on groups	31	30	37	17	12	127
No. of stock transfers	33	6	29	15	13	96
No. of partners <sup>2</sup>	17	24	13	8	10	72
Average size of RSL in units	5,165	5,940	6,745	5,311	4,421	5,674
With less than 2,500 units	44	41	36	22	14	157
Between 2,500 and 5,000 units	21	14	22	13	12	82
Between 5,000 and 10,000 units	26	9	18	10	8	71
Greater than 10,000 units	12	14	20	10	5	61

Table 3: Actual efficiency gains 2005-06

£ million	Total achieved	CLG Targets	Variance £ million
Capital works	81	2	79
Management and maintenance	130	35	95
Commodities	27	10	17
Other	80	N/A	80
<b>Total</b>	<b>318</b>	<b>47</b>	<b>271</b>

<sup>2</sup> Investment partners are defined as those lead partners in the 2006-08 National Affordable Housing Programme..

Graph 1: Share of efficiency gains per each regulation field



### Summary of gains for 2005-06

The reported efficiency gains for 2005-06 totalled £318 million split by four areas (Table 3). Since ‘other’ savings do not fall within the Government’s procurement work stream, no target is set. Excluding this area, associations achieved efficiency savings in 2005-06 of £238 million which exceeded the government targets of £47 million by £191 million.

Total efficiency (work stream) gains represent 3.5% of yearly turnover and 4.0% of yearly operating expenditure (including capitalised works to existing stock).

### Efficiency gains recorded by associations in each regulation field

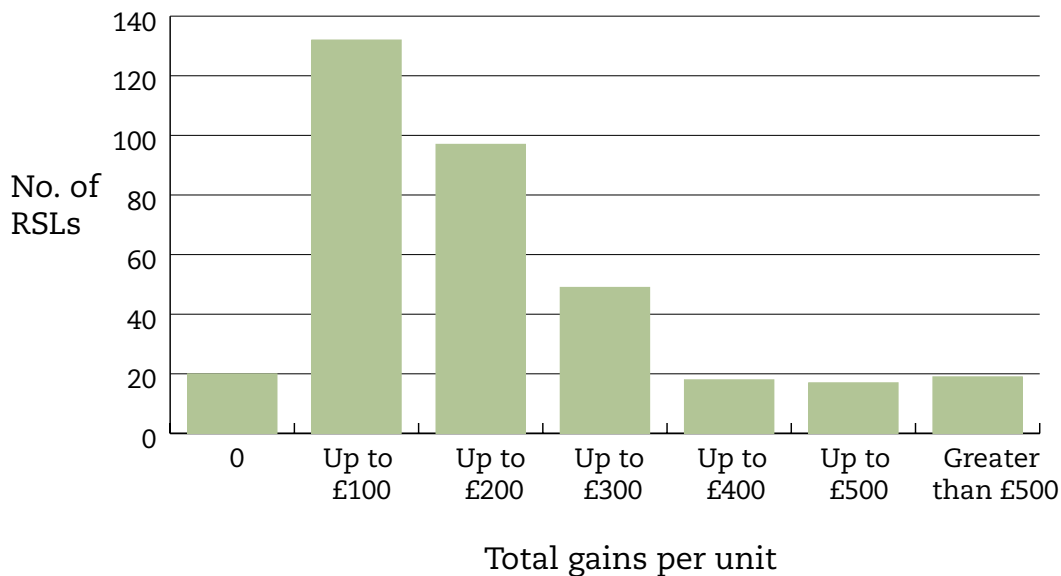
When analysed by location of association (from which field it is regulated) management and maintenance produced the biggest savings in all fields, except in the South East where the greatest efficiency gains were recorded as ‘other’ (Graph 1). Where detail was given, these ‘other’ savings related to treasury management activity and efficiencies derived from organisational restructuring. The greatest gains were recorded by North-based associations across all work stream types. Northern associations

represent some 47% of the total gains recorded for capital works.

The relative share of the savings attributable to each field is determined largely by the relative numbers and attributes of associations in each field as set out in Table 2. North field associations clearly achieve a higher proportion of the savings compared to the other fields. However, this is to be expected. The average size (by unit) of North field regulated associations is higher than

elsewhere in the country; it has a third of the largest groups or individual associations (with greater than 10,000 units) and larger associations achieve greater efficiency savings in total. Also North field associations include a significant proportion of the newly registered stock transfers, which tend to achieve comparatively high efficiency gains in capital works. In total, associations regulated from the North field achieved 38% of the savings recorded, London and Central associations 22%, South East associations 12% and South West associations 6%.

**Graph 2: Range of per unit savings**



## Savings per unit

When analysed by average work stream savings per unit (Table 4), (excluding savings classified as other) stock transfers produce the largest savings.

Analysis by size (unit) of associations reveals that those associations with less than 2,500 units, whilst making the smallest overall contribution to the level of sector

gains, delivered the highest gains per unit. There did not appear to be any one overriding driver behind this characteristic, although savings from small scale mergers, improvements in void loss and more challenging negotiation over the cost of supply of goods and services appeared to be factors influencing this outcome.

A number within this grouping observed that gains per unit would have been higher

**Table 4: Analysis of savings per unit**

2005-06 efficiency gains	Average work stream savings per unit £	Average total savings per unit £	Contribution to total work stream gains £m
All RSLs	121	162	238
Stock transfer RSLs only	145	178	108
All RSLs excluding stock transfers	113	157	130
Lead investment partners only	98	160	57
RSLs with less than 2,500 units	141	187	18
RSLs with between 2,500 and 5,000 units	98	138	30
RSLs with between 5,000 and 10,000 units	109	130	52
RSLs with greater than 10,000 units	119	171	138

if gas and electricity charges had not risen substantially over the last 12 months. This was a factor to which a number of larger associations also drew attention.

For associations with more than 2,500 units, size did not appear to be a significant factor in the level of gain per unit generated. Those associations with more than 10,000 units delivered well over half of all the sector gains for the year, £138 million out of the £238 million work stream total and £189 million of the total gains of £318 million, whilst representing only 16 % of the returns.

The average per unit saving recorded for each sub-set of associations will obviously mask the differing range of savings recorded by individual associations. At an individual level 20 associations returned a nil net efficiency gain in the year and a further 20 recorded a net loss or inefficiency. Of those that did generate a gain most reported gains of up to £100 per unit as shown in Graph 2.

## Other efficiency gains

From this analysis, gains attributed to 'other' (i.e. non procurement work stream savings) represent a significant proportion of the total

efficiencies achieved to date, some 25%. We undertook analysis of the savings recorded as 'other' to understand the activities contributing to these significant savings. Around 70% of associations recorded 'other' gains in the AES.

Whilst returns did not always identify the source or value of the area in which the gain had been achieved a significant proportion of associations referred to savings in treasury management. Efficiency gains in this area include refinancing of the current portfolio, achieving tighter margins, lower fixed rates and the use of hedging, rather than simply the effects of variation in base rate consequent impact on interest cost. Although a precise figure is difficult to determine from the returns, approximately £27 million of 'other' gains related to treasury activity.

A number of associations recorded their recurring savings from last year's backward look in 'other' gains. This was probably due to the format of the pro-forma which did not allow for savings occurring in 2005-06 to be added to the brought forward recurring savings. Since the yearly targets set reflect the increased efficiency over the base year

calculation, we have amended the pro-forma to enable associations to clearly recognise the total savings achieved and recurring to allow full reporting of total savings against the targets.

Interestingly, a number of associations also recorded gains from improved void performance and arrears management in 'other' whilst the majority included these types of gains in the management and maintenance work stream. Improvement in void and arrears management is specifically mentioned in the key areas for efficiency gains and associations should therefore record these gains within the management and maintenance work stream.

Similarly, associations referred to improvements in insurance portfolios as an 'other' gain. Again this area is specifically mentioned as a possible area for efficiency gain within the commodities work stream and should therefore be reflected there.

## Recorded inefficiencies

Within the AES returns for a number of associations, reference is made to efficiency losses which are netted off against the value of gains achieved at an individual

association level. For some associations, the losses recorded are in excess of efficiency gains recorded either on an individual work stream level or in total.

The value of losses identifiable from the AES returns total £33.5 million, thus reducing the value of all gains by 9.5%. However this figure is likely to be understated since a degree of netting of losses against gains will happen at sub work-stream level.

Twenty returns showed overall total losses, represented by two stock transfer (10%) and 18 traditional associations (90%). However the overall losses from stock transfers is proportionately smaller at £0.5 million (1.4%).

A range of explanations was provided for the losses (Table 5) and some are clearly due to upfront costs which are intended to produce longer term efficiency gains.

Whilst there will be areas where unforeseen expenditure over that planned occurs, it appears that a number of losses recorded relate to volume differences – in that works or planned expenditure was brought forward. It is possible that incorporating those volume changes in the calculation

for efficiency may result in reduced recorded inefficiencies. It is important also that associations recognise any losses by reference to the services delivered and

volumes achieved in the base year. Several of the losses identified appear to be overstated since recurring savings were not included within the AES return.

**Table 5: Examples of the areas incurring losses**

Capital works losses	Management and maintenance losses
<ul style="list-style-type: none"> <li>• brought forward capital works</li> <li>• unforeseen costs</li> <li>• reduction in capital work uplift</li> <li>• scheme environmental works</li> </ul>	<ul style="list-style-type: none"> <li>• increased subcontractor costs</li> <li>• unplanned legal fees</li> <li>• restructuring costs</li> <li>• employment of agency staff</li> <li>• ramifications of stock lost to Right to Buy</li> </ul>
Commodities losses	Other losses
<ul style="list-style-type: none"> <li>• big increases in energy costs</li> <li>• increased overheads (no details)</li> </ul>	<ul style="list-style-type: none"> <li>• higher than expected interest</li> <li>• increased overheads</li> <li>• unexpected legal costs</li> <li>• merger costs</li> </ul>

# Achievement compared to forecast

The £318 million efficiency gains for the year ended 31 March 2006 achieved by associations was approximately £7 million lower than predicted in the previous year's AES.

Table 6 below shows the contribution by each work stream to the total gain and the level of variation between the projected level of efficiency and outturn at individual work stream level.

At an individual association level there was a high degree of volatility and less than 15% of all associations reported variances within +/- 10% of their predicted gain for the year. Similarly associations reported high levels of variance in relation to outturn on individual work streams. One association reported gains in the management and maintenance work stream of over £6 million compared with a planning total of less than £1 million.

In contrast another association, again for the management and maintenance work stream reported a loss approaching £0.5 million compared with a planned gain of nearly £1.5 million.

Our review of the associations' AES returns indicated that the main reasons for variance across each of the work streams was as follows:

## Capital works

Not unexpectedly, associations highlighted the fact that savings were lower than anticipated in last year's forward look because of the reduction in the allowed uplift for capital works. A typical quote from one association's AES illustrates this point: "We did not achieve the cost savings of £2.4 million for capital works. Our estimate of efficiency savings were almost entirely based

**Table 6: Comparison of efficiencies achieved to forecast**

Work stream	Projected 2005-06 gains £m	Actual 2005-06 gains £m	Variance %
Capital works	98	81	(17)
Management and maintenance	117	130	11
Commodities	23	27	17
Other	87	80	(8)
Total	325	318	(2)

on achieving lower price increases than the 11.0% inflation used as the guideline in July 2005. Our current calculations are re-based for July 2006 on the current inflation guideline of 4.1%. We estimate that prices, based on schedule of rates from our suppliers, are approximately the same for both years. We therefore report no efficiency gain or loss for the year on our capital programmes.”

Those associations reporting actual gains higher than assumed indicated that this was mainly due to a greater volume of works being undertaken than planned for at the outset.

### **Management and maintenance**

A majority of associations reported gains greater than predicted at the start of the year. Those reporting the largest positive variances attributed this to proactive restructuring activity leading to a combination of staff savings and reductions in overhead costs. Other associations tended to highlight the benefits accruing from reviewing their repairs and maintenance functions as well as a combination of miscellaneous factors including a reduction in void loss and re-let times, and savings on

insurance premiums following re-tendering. Those associations reporting negative variances pointed to the repairs activity being greater than expected and over ambitious planning assumptions.

### **Commodities**

This work stream generated the lowest level of reported gains. Those associations delivering gains above target in this area highlighted service improvements as having a positive impact as well as staffing costs being lower than planned.

### **Other**

Associations reported significant volatility between actual outturn and predicted gain at the start of the financial year. As an example, one association reported a £4.5 million loss compared with a planned gain of £100,000. This was due to increased office occupancy costs following a rationalisation, although the association expected this action to enhance the level of future gains. Associations reporting the largest gains attributed this to treasury management savings as well as savings in VAT and other costs from reviewing their internal arrangements.

# Forecasts for 2006-07

Table 7 below shows the targets set by CLG for 2005-06 and 2006-07 by work stream, and compares these to the forecasts made by the housing association sector for these two years.

The total sector forecasts for 2005-06 and 2006-07 are substantially greater than the targets set by CLG for those years. The magnitude of the difference varies considerably within each work stream but a notable exception is the sector forecast for commodities in 2006-07 which is just

at the target for this work stream. Many associations refer to the difficulties in achieving efficiencies in this area (both the forward look and backward look) which commonly include reference to:

- the sharp increase in 2006 in fuel costs, such as gas and electricity. This is most noticeable among those associations with a substantial number of sheltered schemes, care homes or other types of communal accommodation;

**Table 7: Comparison of forecasts to the Department's targets**

Work stream	CLG target 2005-06	Sector forecast 2005-06	Variance	CLG target 2006-07	Sector forecast 2006-07	Variance
	£m	£m	£m	£m	£m	£m
Capital works	2	98	96	30	86	56
Management and maintenance	35	117	82	60	138	78
Commodities	10	23	13	30	30	0
Work stream totals	47	238	191	120	254	134
Other <sup>3</sup>	0	87	87	0	94	94
Total	47	325	278	120	348	228

<sup>3</sup> No target is set for other gains

- where procurement gains predicted for 2005-06 failed to be achieved, leading associations to lower their expectations for gains in this work stream for 2006-07;
- where associations have achieved substantial efficiency gains in commodities in the last two years and now wish to consolidate these gains while focusing on maintaining or improving customer satisfaction; and
- where procurement-related efficiency initiatives (for example joining Procurement for Housing) have yet to become effective.

Table 8 provides an analysis of the frequency of occurrence of efficiency savings greater than £1 million by individual associations

in any of the work streams. It shows that management and maintenance was the most popular area with 29 occurrences in 2005-06 and 36 occurrences forecast for 2006-07. Not unsurprisingly, commodities feature the smallest number, where there were seven occurrences of £1 million-plus efficiency gains in 2005-06 and eight forecast in 2007-08.

Table 9 provides an analysis of forecast efficiency gains by field of regulation for each association and shows that 37% or £98.5 million of the total of all gains are forecast to be delivered by associations in the North field. This is largely consistent with the comparable actual outturn for 2005-06.

**Table 8: Incidence of £1 million savings recorded in a return**

Work stream	No. of associations forecasting a gain of over £1 million	
	2005-06 forecast	2006-07 forecast
Capital Works	26	16
Management and maintenance	29	36
Commodities	7	8
Other	18	22

Table 9: Forecast gains by location

Forecast gains 2006-07	Capital works (£m)	Management and maintenance (£m)	Commodities (£m)	Other (£m)	Total (£m)	% Share
Central	12	30	4	16	62	18%
London	16	38	5	39	99	28%
North	44	45	16	24	129	37%
South West	6	5	1	4	16	5%
South East	7	21	3	11	43	12%
Total	86	138	30	94	348	100%

## Comparison of forecasts to targets by each work stream

### Capital works

The capital works work stream shows the greatest variance between CLG's targets and sector forecasts, with the sector forecasting gains many times greater than the target in both years. Eleven associations forecast that they would achieve the £2 million target set by CLG in 2005-06 with their efficiency gains alone. This is most likely due to the sheer scale of associations' investment in stock as

a consequence of programmes set in place to meet the Decent Home Standard and re-improvement works undertaken by stock transfer associations. The scale of capital works spend, both in absolute terms and as a proportion of total costs, are increasing and the review suggests that many associations had initiatives in place to achieve more efficient procurement of works, to ensure the programmes are deliverable. The 2006-07 target is significantly higher than the previous year's, although there is one stock transfer association that has itself forecast gains of almost 50% of the total target.

Almost 60% or £50.3 million of capital works efficiencies are projected to be delivered by stock transfers. This is a disproportionately large percentage compared to the distribution of stock transfers in the sector. However, given the extent to which catch-up repairs and refurbishment programmes feature in the business plans of this peer group, it is to be expected that this will also be the largest single source of their efficiency gains.

### Management and maintenance

The management and maintenance work stream is the source of the largest efficiency gains in absolute terms. The sector forecast in 2005-06 of £117 million was over three times the target set by CLG for that year of £35 million. The target for 2006-07 has almost doubled. Nevertheless, the sector forecast, at £138 million, is higher than the previous year indicating that this area will continue to be a source of substantial efficiency gains.

Investment Partner associations are projecting to contribute some 30% or £41.5 million of management and maintenance gains which is disproportionately more than

would be expected. This may well indicate that because associations in this peer group are the most active in terms of business growth and exposure to new opportunities, they have more scope to reconfigure their operations to generate efficiency gains.

### Commodities

The sector forecast for 2005-06 was £23 million which is more than double the £10 million target set by CLG. The target for 2006-07 is considerably increased and sector forecasts have only just matched this. The sector has clearly found it particularly challenging to deliver for this work stream.

### Other

No targets are set by CLG in this area. We have found that the sector made substantial efficiency gains in 2005-06 in this non-specific work stream and expects to continue delivering in 2006-07.

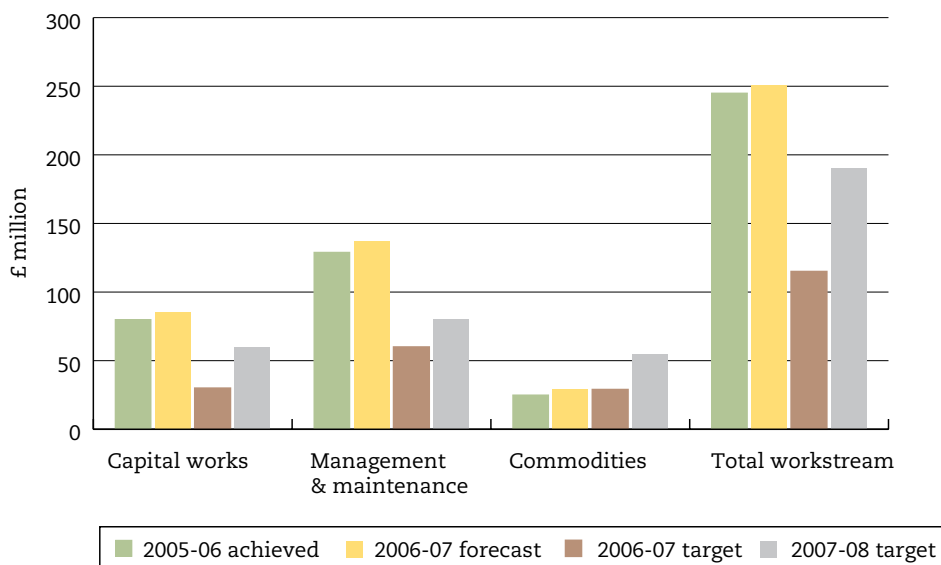
A significant source of efficiency gains forecast in 2006-07 continues in treasury management initiatives such as refinancing loans to reduce the cost of servicing debt.

### Forecasts and targets compared to outturn efficiencies achieved to 2005-06

Perhaps the most significant issue arising from associations' forecasts for 2006-07 is the extent to which they have changed only incrementally from last year's forecasts and actual gains achieved. However, the sector's total forecast gains for 2006-07 are 6.7% ahead of efficiencies recorded in 2005-06 and significantly exceed the interim 2006-07 CLG targets.

Graph 3 below demonstrates both the extent to which associations' achievements to date and forecasts in the main far exceed CLG's targets but also highlights the comparatively marginal increase in gains forecast for 2006-07 compared to the substantial gains achieved in 2005-06.

**Graph 3: Forecast increase in efficiencies in 2006-07**



Considering the efficiencies achieved in 2005-06 and those forecast in 2006-07 it appears the sector is well placed to meet the target for increased efficiency of £195 million per year by 2007-08. Forecast gains for 2006-07 exceed CLG's targets set for both 2006-07 and 2007-08 in both the capital works and management and maintenance work streams. However, the target for commodities appears more challenging for the sector. Whilst the interim target for 2006-07 is forecast to be met, the third year target of £55 million represents an 83% increase in efficiency per year above the level reported in 2005-06 and forecast for 2006-07.

The tremendous achievement of gains reported in the first year reflects the fact that the sector was engaged in seeking improvements in efficiency as a consequence of key policies such as rent restructuring and compliance with the Decent Home Standard which, for many, have put operating margins under pressure. The forecast for additional gains in 2006-07 are comparatively more cautious. There is however some doubt about the extent to which recurring savings are included (potentially causing an understatement of gains) and we have ensured the reporting format for 2006-07 facilitates capture of that information.

However, future opportunities for improvements in efficiency will likely be realised through the procurement initiatives supported with the efficiency fund, which will take time to operate fully. Similarly, the continuing merger and restructuring activity in the sector should release further efficiencies over the longer term as more efficient and effective organisations result over the longer term.

### **Other performance information**

In undertaking the sense checks on AESs and formulating the dataset for the analysis, we have introduced a range of information including key performance indicators, inspection results and financial information. The aim of introducing this information is to facilitate the identification of outliers, key trends or relationships and any conflicting information.

There are however a number of limitations in interpreting the different range of information we collect. AES returns are required at association group level; conversely we collect performance indicator information at individual association level and inspections may be undertaken for a specific part of a group only. Therefore, in interpreting AES savings alongside other

information, we assess the performance of the group as a whole, by reference to an assessment of the group's parts.

We tested a number of indicators across the data set to search for any correlation between the data and identification of outliers or results that appeared contradictory. The indicators included:

- financial information on turnover and operating expenditure (and AES gains as a proportion) in total and per unit;
- operating cost index results;
- Decent Home Standard;
- re-let time;
- voids;
- tenant satisfaction; and
- date and result of latest inspection.

The financial information was important in identifying those associations that appeared to be outliers in performance. Investigation of these outliers tended to confirm that the AES return was not completed in a manner consistent with other associations – and usually because the pro-forma was not used. We were therefore able to focus on those AESs that appeared as outliers and clarify the information reported.

Unsurprisingly, there was a high correlation between the total gains recorded in 2005-06 and size of association, whether determined by unit number, turnover or total operating expenditure. However, when per unit comparisons were made, there was no meaningful correlation. This bears out the result of the analysis that the size of an association does not affect the extent to which it is achieving efficiency gains, either as a percentage of total expenditure or on a per unit basis.

Forecast gains were not highly correlated to gains achieved, which suggests that either the gains achieved in 2005-06 contain one-off gains or, more likely, the full extent of recurring gains has not been recorded in either of the forecast for 2007-08 or the actual efficiencies in 2005-06.

The actual efficiency gains reported calculated on a per unit basis were analysed alongside other performance indicator (PI) results for 2005 and 2006, including both financial and non financial indicators. No correlation was found between any of the indicators and the efficiency savings. This is particularly interesting for the per unit operating cost and investment in stock performance indicators and the operating

cost index. There is no correlation between the results for the financial cost per unit PIs and the savings per unit. Therefore there is no indication that comparatively high cost associations are achieving greater or lesser efficiency savings than low cost associations. This is not however an anomalous or counter intuitive result. Associations are encouraged to reapply efficiency gains secured to front line services, increasing the quality or range of those services. There is no presumption therefore that the efficiency savings will result in reduced operating costs. Some associations do state however that some degree of the resources released by efficiencies will be applied to capital projects.

A review of the national performance indicator results for 2006, compared to 2005 does not indicate that those associations achieving the most significant efficiency gains per unit were doing so to the detriment of service delivery. The 100 associations with the highest per unit efficiency gains were analysed to see whether their performance across a range of PIs has improved or deteriorated during 2006, compared to all associations PI results. This analysis is problematic since, for

example, tenant satisfaction is currently measured once in three years, and we would not therefore necessarily expect to see change and difficulty in mapping individual association PI results to AESs reported at a group level. However, results indicate that the percentage of these associations improving performance in each PI was similar to the associations across the board.

Associations are required to ensure that efficiency gains are not made at the cost of the quality of service delivery. To do that, associations need to establish or build in existing performance monitoring and ensure it is at the right level to measure quality improvements. This will require performance monitoring at a more local level than for example those indicators included as a Corporation key PI. The pro-forma AES return provides associations with the opportunity to confirm how they monitor standards.

In addition to sense checking the AES returns against performance indicators, we have developed a methodology for looking at the operational efficiency of associations in the round, to help inform our understanding of financial capacity.

The process brings together PI information, comparative operating cost information, the Operating Cost Index (OCI), the results from inspections and AES financial and non financial information together with our knowledge of associations' business strategies and seeks to identify outliers in areas of operational performance. This is focussed largely on those associations in receipt of significant Social Housing Grant and is intended to help focus discussions we may have with associations in helping to continue to drive efficiency in new supply.

# Appendix: Good practice case study examples

## Value for money (VFM) strategy

Efficiency is not a new area of focus for housing associations. The desire to provide excellent quality services, whilst clearly demonstrating value for both residents' and tax payers' money, is not new. However, this form of activity covers a broad range of associations' activities and will need an overarching strategy to ensure that the Board has ownership of the organisation's approach and that this is understood at all levels. There were many examples of good practice and clear use of the strategy as an improvement tool.

procurement is made available for all staff, so that staff feel confident in making purchasing decisions. The association has in place a system of delegated authorities and Board approvals. Finally, the association is a member of the procurement agency OGC Buying Solutions, an Executive Agency of the Office of Government Commerce in the Treasury.

## Case study: Agudas Israel HA

Agudas Israel HA (AIHA) is a Black and Minority Ethnic (BME) association, based in North London, with a current stock profile of just over 450 homes. Their VFM strategy as outlined in their AES was particularly comprehensive and demonstrated a sense of being 'owned' at all levels of the organisation. AIHA is a member of the Soloman group, which is a consortium of smaller associations based in London. The group assists members to deliver service improvements by sharing good practice and resources. In this instance, AIHA worked with other members of the group to carry out Best Value reviews. Training on effective

## Resident involvement

The importance of customer focused service delivery is paramount for the housing association sector and has been of increasing importance to the Housing Corporation over the last two years. We have specifically asked associations in the AES template to offer some narrative on how they are involving their residents in their discussions on value for money priorities. There has been some concern in the sector that efficiency gains will be at the expense of the overall quality of services that residents experience. Therefore involving residents in a meaningful sense in VFM discussions will help ensure that this is not the case. It also allows associations to build up the capacity of residents (at both individual and collective level) to more fully appreciate how associations carry out their business and operational planning activities.

## Case study: First Wessex Housing Group

First Wessex Housing Group was formed in 2005 from the merger of two housing associations and has a stock of approximately 10,000 homes. The group has recently adopted a new Customer First strategy, which looks at resident involvement in all areas of the group's activities. One aspect of the strategy is the formation of four Business Improvement Groups, comprised of board members, staff and residents. These groups will be reviewing stock investment and asset management, housing services, supported housing services and strategic development and resources. The work of the groups will be supplemented by other approaches to improving service delivery through involvement, such as focus groups, customer surveys and mystery shopping.

## Monitoring service standards

The need for effective monitoring of service standards is linked to the above – we need to have absolute certainty that the gains being achieved by associations are not at the expense of the quality of service provision. Whilst the involvement of residents is critical, associations will need to ensure that they have in place high calibre monitoring and management information, to track trends in performance. The fourth area of case studies (maintaining standards) is linked to this area of assessment.

## Case Study: Metropolitan Housing Partnership (MHP)

MHP is one of the largest associations in the country, owning over 26,000 homes in the East Midlands and the South of England. The partnership employs a range of measures to monitor efficiency:

- MHP is a founder member of the HouseMark G15+2 benchmarking club. HouseMark is used to benchmark the cost and performance of frontline services;
- as part of the annual business planning and budgeting cycle, cost and performance data for individual businesses within the Partnership are considered against internal and external benchmarks to ensure that resources are allocated appropriately;
- the Partnership benchmarks itself against other associations within those regions where MHP provides services and uses this benchmarking process to improve performance;
- The Partnership’s Strategic Assessment of Results and Targets is prepared each month and presents performance trends against financial and non-financial measures to ensure that services are being efficiently delivered against planning targets;
- monthly management reports are prepared for finance and other activities to ensure that efficiency plans set at the start of the year are being achieved. The Partnership also reviews unit costs across the business to understand cost differences and ensure that best practice is shared. Involvement of residents is vital to ensuring the linkage between output quality and costs.

## Reinvestment of gains

Sir Peter Gershon's work was underpinned by the Government's commitment to ensuring that frontline public sector services are of an exceptionally high quality. His intention was to ensure that efficiencies made in back-office functions were recycled to the frontline. We were particularly keen to look at this area in some depth in the second year of the efficiency programme, as this would obviously be when some of the gains would start to make a real difference to service provision.

families moving into Derwent's stock); a counselling and therapy service for children living in the association's refuge in Derby and a contribution towards the cost of the neighbourhood warden scheme in Ashfield.

## Case study: Derwent Living

Derwent is a medium sized association, providing a diverse range of activities and services, predominantly in the East Midlands. Its AES indicated gains of just over £960,000. The association regards the provision of affordable housing without grant as being a vital supplement to SHG funded activity and sees its future profitability as being a necessary component of delivery of housing via this route. The association's Social Investment Fund is also supplemented by the reinvestment of efficiency gains. In 2005-06, the Fund was used to cover the recruitment of a Family Welcome Officer (to provide support to new

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