NSW Registrar of Community Housing

Financial Viability Implications for Community Housing Providers – COVID-19

Document Owner – Registrar of Community Housing
Final Copy released July 2020

PURPOSE

To measure the likely short term financial impact on community housing providers' (CHPs) operating performance, liquidity, and capital structure measures through a sensitivity analysis based on a potential loss of rent revenue due to COVID-19.

EXECUTIVE SUMMARY

The NSW Registrar of Community Housing (Registrar) undertook a preliminary sensitivity analysis on the likely short term impact on financial viability in the community housing sector as a result of the potential loss of rent revenue due to COVID-19.

This paper and the sensitivity analysis show that the financial impact of COVID-19 arising from the partial or total loss of affordable housing rent revenue will have only a short-term impact in operating performance and that community housing providers will remain solvent.

This paper provides a detailed financial analysis to support the above proposition.

The sensitivity analysis shows the impact upon 18 Financial Performance Reports (FPRs) from Tier 1 CHPs and five FPRs from Tier 2 CHPs (total 23 FPRs) in a range of scenarios:

Base case scenario:	The base case scenario is the forecast 2019-20 and 2020-21 as submitted in the FPR by each of the 23 CHPs as part of the compliance assessment.
Scenario 1:	Rent Revenue Reduction Rate of 10% for Affordable Housing and 0% for Social Housing.
Scenario 2:	Rent Revenue Reduction Rate of 30% for Affordable Housing and 0% for Social Housing.
Scenario 3:	Rent Revenue Reduction Rate of 100% for Affordable Housing and 0% for Social Housing.

FPRs used in this sensitivity analysis have different proportions of affordable housing within their housing portfolios that directly affects the financial impact of rent revenue reduction.

11 FPRs (or 61%) of Tier 1 CHPs have affordable housing proportions above 10% and four FPRs (or 22%) have affordable housing proportions above 30%. Two FPRs (or 40%) of Tier 2 CHPs have affordable housing proportions above 25%.

This analysis does not contemplate alternative strategies that CHPs could potentially use to mitigate the loss of affordable housing rent revenue and potential damage to operating performance. For example, replacing affordable housing tenants with other affordable housing tenants, use the property to provide social housing or other type or housing, delay development projects, or sell affordable housing owned properties.

The aggregated Tier 1 FPRs would remain stable as the reduction in affordable housing rent revenue would have an immaterial financial impact on operating income and liquidity in all three scenarios in 2019-20. Average performance of operating margin ratios and liquidity ratios remain above National Regulatory Code thresholds in all scenarios.

The aggregated Tier 1 FPRs would remain stable as the reduction in affordable housing rent revenue would have an immaterial financial impact on operating income and liquidity in

scenario 1 and scenario 2 in 2020-21. Average performance of operating margin ratios remain above National Regulatory Code thresholds in scenario 1 and below threshold but still positive in scenario 2.

The aggregated Tier 1 FPRs have a material impact on operating income and overall operating performance in scenario 3 in 2020-21. The impact on liquidity is not material. The damage on operating performance is so significant that it could generate threats to short-term viability if any other variable, as explained in the assumptions section, does not change.

The aggregated Tier 2 FPRs would remain stable in all three scenarios in 2019-20 and 2020-21. The overall financial impact is not material across the two forecast years.

Individual FPRs presenting a combined underperformance in measures related to operating performance, liquidity, cash flow, and interest cover ratio (ICR) would be assessed on a per case basis on its own merits. The degree of financial impact on each CHP depends on the proportion of affordable housing to the overall housing and the size of the provider.

CHPs have strong balance sheets. This means that they have robust total asset and net asset positions that allows them to develop strategies and/or mitigate financial risks from perilous financial performances created by the loss of rent revenue in affordable housing due to COVID-19 and to remain viable or solvent for the foreseeable future.

Most CHPs have expressed little or no concern about the immediate financial impact of reduced rent revenue or rent arrears in 2019-20.

Several CHPs report that their income from affordable housing has remained stable largely as a result of government initiatives designed to minimise the economic impact of COVID-19. However, the situation could change significantly when these programs are wound back.

After completing the sensitivity analysis in addressing the financial impact derived from the partial or total loss of affordable housing rent revenue due to COVID-19, the results from the scenario analysis indicate that the aggregated 23 FPRs would have only a short-term impact in operating performance and viability and that providers will remain solvent for the foreseeable future.

BACKGROUND

The community housing sector in NSW provides social and affordable housing for people on very low to moderate incomes that is generally managed by not for profit CHPs.

COVID-19 has impacted the community housing sector in NSW as it has every other sector in the community. The inability of tenants, primarily those who are not on statutory benefits, to continue paying rent will have a financial impact on individual CHPs resulting by way of a loss of rent revenue.

COVID–19 is a virus that has spread rapidly across Australia and the whole world, infecting a large number of people and, unfortunately, causing many casualties since January 2020.

The Australian Federal Government and the NSW Government have each taken the necessary measures to stop the virus from spreading and minimising the number of casualties. These measures have inevitably had an impact on the economy. Many economic sectors and industries have been and continue to be affected by the temporary closure of businesses and social distancing measures. The unemployment rate is increasing although the Federal Government has implemented economic incentives to support affected businesses and employees.

INTRODUCTION

The Registrar undertook a sensitivity analysis to consider the implications on the short term viability of the community housing sector derived from the potential loss of rent revenue due to COVID-19.

It is an object of the *Community Housing Providers (Adoption of National Law) Act 2012* NSW to ensure that "registered community housing is developed as a viable and diversified component of the NSW social housing sector"

The National Regulatory Code (Code), which is an appendix to the National Law, sets out the performance outcomes and requirements that must be met by registered CHPs under the National Regulatory System for Community Housing (NRSCH). Once registered, CHPs must demonstrate ongoing compliance with the Code. Financial Viability is one of the seven performance outcomes for housing providers under the Code. CHPs are assessed against three performance requirements: ensuring a viable capital structure, managing appropriate financial performance, and managing financial risk performance.

The FPR is a National Regulatory System tool used to collect financial information and to assess the financial viability of CHPs. The FPR includes prudential financial viability measures that provide an input to the financial performance assessment under the National Law and the Code, and supplement the Evidence Guidelines, which can be found on the Registrar's website.

The financial measures include performance thresholds for some requirements as an indicative guide to assessing performance results. The thresholds do not determine capacity or compliance per se. Rather, they provide a transparent level of performance as a starting point against which results can be assessed. The following table shows the thresholds required to be met under the National Regulatory Code.

Financial viability measures	Threshold			Data Definition
	Tier-1	Tier-2	Tier-3	
Operating EBITDA Margin	>=8%-15%	>=3%-10%	0% - %5	• Operating EBITDA(Earnings before interest, tax, depreciation and amortisation) / Operating Revenue*
Working Capital Ratio	>=1.5 times	>=1.5 times	>1.5 times	• Current Assets less unspent capital grants / Current Liabilities less capital grants received in advance and accommodation bonds
Amended Quick Ratio	>=1.2 times	>=1.2 times	>1.2 times	• Cash, Short-term investments & unused overdraft facilities / Current liabilities less capital grants received in advance and accommodation bonds
Operating cash flow adequacy	>=1.20	>=1.05	>1.00	• Operating Cash Inflows / Operating Cash Outflows
Gearing Ratio	<=30%	<=30%	<30%	• Total repayable debt / Total assets
Interest cover	>=1.5 times	>=1.5 times	>1.5 times	• Operating EBITDA / Financing costs
Debt serviceability	Trend	Trend	Trend	• Repayable debt / Operating EBITDA - finance costs
Return on assets	>=5%	>=5%	>5%	• Operating EBITDA / Average total assets
Cash cost of capital	<=2.5%	<=2.5%	<2.5%	• Total finance costs/ Average total assets

*Operating revenue excludes capital grants and non-cash income

SCOPE OF THE ANALYSIS

The scope of this analysis is for the forecast years 2019-20 and 2020-21. The intention is to measure the short term financial impact in operating performance, liquidity, and capital structure measures.

The analysis focuses mainly on the potential loss of income from affordable housing tenants affecting their ability to pay rent to CHPs, thereby generating a reduction in rent revenue.

It was not possible to differentiate affordable housing tenants receiving statutory income from tenants receiving a low salary. The reduction in rent revenue is taken into account irrespective as to whether the tenant is on a low or statutory income. What is relevant is that they are an affordable housing tenant.

Tenants who only receive statutory income and pay affordable or social housing rent as set by the Government have housing security and should continue paying their full rent. This is a working assumption in this paper.

One CHP expressed concern about placing a moratorium on all residential housing evictions being considered as part of the emergency response to COVID-19. This may cause a potential impact in social housing rent revenue if tenants stop paying rent immediately. The “no eviction” policy for social housing tenants would operate as an incentive for tenants to stop paying rents. This would have a further material impact on rent arrears, rent collection and ultimately cash balance. This paper does not take into account the impact, if any, of tenants on statutory benefits who choose not to pay their rent.

The sensitivity analysis is based on contemporary financial data as part of the current round of compliance assessments. Forecast figures used in this analysis were submitted between December 2019 and April 2020.

The sensitivity analysis considers 23 FPRs that represent 25 Tier 1 & 2 CHPs. One of the CHPs has a parent and two subsidiaries registered under the National Regulatory System but submits one FPR with consolidated figures.

The FPRs considered in this analysis are as follows:

FPR	Tier	Affordable	Social	SDA
1	Tier 1	17%	83%	0%
2	Tier 1	3%	97%	0%
3	Tier 1	45%	55%	0%
4	Tier 1	12%	87%	1%
5	Tier 1	96%	4%	0%
6	Tier 1	17%	82%	1%
7	Tier 1	13%	85%	2%
8	Tier 1	31%	67%	2%
9	Tier 1	1%	99%	0%
10	Tier 1	9%	82%	9%
11	Tier 1	11%	84%	5%
12	Tier 1	13%	87%	0%
13	Tier 1	99%	1%	0%
14	Tier 1	5%	95%	0%
15	Tier 1	16%	83%	1%
16	Tier 1	8%	92%	0%
17	Tier 1	7%	93%	0%
18	Tier 1	4%	96%	0%
1	Tier 2	30%	70%	0%
2	Tier 2	0%	100%	0%
3	Tier 2	0%	100%	0%
4	Tier 2	26%	74%	0%
5	Tier 2	0%	100%	0%
23 FPRs				

The breakdown of affordable housing, social housing, and specialist disability accommodation (SDA) is based on property numbers. The percentages presented in the table above are an approximation based on best information available. The source of information is primarily property data level, if available, annual reports and strategic asset management plans.

11 FPRs (or 61%) of Tier 1 CHPs have affordable housing proportions above 10% and four FPRs (or 22%) have affordable housing proportions above 30%. Two FPRs (or 40%) of Tier 2 CHPs have affordable housing proportions above 25%.

ASSUMPTIONS OF THE SENSITIVITY ANALYSIS

The decrease in rent revenue will have an immediate impact on EBITDA and cash inflows, and hence affect cash balance. The scale of this impact will provide an indication of the CHP's readiness to respond to assumed loss of revenue. In the normal course of events after the tenant stops paying rent, a rent arrears balance is created together with a receivable account. If rent arrears are not recoverable or recovered, then it turns into a bad debt with the tenant at risk of being evicted.

Besides rent revenue, cash inflow, and cash balance, all other variables remain unchanged in the course of the analysis. The analysis does not cover the cost of restructuring measures that each CHP may put in place to offset the effects of loss of rent revenue. Cost restructuring is the process of reorganising operating costs to improve the long-term profitability and efficiency of a company.

It is acknowledged that CHPs may also have unforeseen savings or expenses if they have been directly affected by COVID-19. These unforeseen transactions are unknowable and hence form no part of the sensitivity analysis.

The decrease in rent revenue has had an impact only in the last quarter of the forecast year 2019-20 and a possible full financial year impact in 2020-21.

The dollar value proportions of affordable housing rent revenue, social housing rent revenue, and SDA rent revenue for each of the CHPs are the same as the proportions shown in the table above which were obtained based on property numbers.

The proportions of affordable housing units, social housing units, and SDA units are the same for each of the CHPs in 2019-20 and 2020-21.

Affordable housing is the subsector primarily affected by unemployment caused by COVID-19. The effect unemployment has on rental income is mitigated by the assumption that tenants will seek statutory income under relief programs or generally. The sensitivity analysis proceeds on this basis.

Under the NSW Affordable Housing Rent Policy, rent is adjusted to reflect changes in income. For example, a tenant in an affordable housing property becomes unemployed reducing household income as a result. In most cases this would result in the rent calculation changing from a subsidy or market rent to rent calculated as a fixed percentage of income. This in turn reduces the rent payable to a community housing provider. However this is difficult to model precisely and it is likely to affect each provider differently with some CHPs even reporting that they do not expect a significant drop in rental income if this adjustment occurs.

No adjustment has been made to distinguish between affordable housing owned and leased by the CHP and affordable housing managed on a fee for service basis because of the unavailability of such information.

This analysis does not take into account the impact, if any, of tenants on statutory benefits who choose not to pay their rent.

National Rental Affordability Scheme (NRAS) incentives from Commonwealth and State Governments continue flowing to CHPs.

Commonwealth Rental Assistance (CRA) is a component of rent revenue when affordable housing rent is based on statutory income and as such CRA is affected by the percentage impact in rent reduction. The analysis assumes the same decrease in rent revenue whether the household income declines partially or totally.

This analysis does not contemplate alternative strategies that CHPs could potentially use to mitigate the loss of affordable housing rent revenue and potential damage to operating performance. For example, replacing affordable housing tenants with other affordable housing tenants, using the property to provide social housing or other type or housing, delaying development projects, or selling affordable housing owned properties.

SENSITIVITY ANALYSIS

The analysis reviews the financial impact on operating performance, liquidity, and capital structure using viability measures as defined in the Evidence Guidelines. The changing variable is rent revenue from affordable housing only at three different rent reduction rates 10%, 30%, and 100%. Of course, a 30% reduction in affordable housing rent revenue for each of two CHPs will vary depending on the proportion of affordable housing that they have. It will have therefore a differential impact on these CHPs.

Scenarios are defined as follows:

Base case scenario:	The base case scenario is the forecast 2019-20 and 2020-21 as submitted in the FPR by each of the 23 CHPs as part of the compliance assessment.
Scenario 1:	Rent Revenue Reduction Rate of 10% for Affordable Housing and 0% for Social Housing.
Scenario 2:	Rent Revenue Reduction Rate of 30% for Affordable Housing and 0% for Social Housing.
Scenario 3:	Rent Revenue Reduction Rate of 100% for Affordable Housing and 0% for Social Housing.

	Scenario 1	Scenario 2	Scenario 3
FY	AH Rent Reduction Rate		
	10%	30%	100%
19/20	Last Quarter	Last Quarter	Last Quarter
20/21	Full Year	Full Year	Full Year

The rent revenue reduction rate for the forecast year 2019-20 affects only the last quarter of the financial year but the figures and financial measures reported in the analysis are annual figures and measures.

The rent revenue reduction rate for the forecast year 2020-21 applies to the full financial year.

Financial Impact in Forecast Year 2019-20

	Rent Revenue Reduction ($ Millions)	Avg % Reduction in Operating EBITDA	Avg % Reduction in Net Operating Cash Flow	Avg Rent Revenue Reduction as a % of Op Income	Avg Rent Revenue Reduction as a % of Net Assets	Number of financial measures underperforming to NRC thresholds				
						Operating EBITDA Margin	Working Capital Ratio	Amended Quick Ratio	Gearing Ratio	Interest Cover Ratio
Tier 1										
18 FPRs										
Base case	0.00	0.0%	0.0%	0.0%	0.0%	7	2	3	1	3
Scenario 1	-2.40	-2.6%	-7.6%	0.4%	0.1%	8	2	3	1	4
Scenario 2	-7.21	-7.7%	-22.8%	1.1%	0.4%	8	2	3	1	4
Scenario 3	-24.03	-25.6%	-76.2%	3.7%	1.4%	12	3	3	1	6
Tier 2										
5 FPRs										
Base case	0.00	0.0%	0.0%	0.0%	0.0%	1	0	1	1	1
Scenario 1	-0.03	-0.1%	-0.5%	0.1%	0.01%	1	0	1	1	1
Scenario 2	-0.09	-0.3%	-1.5%	0.2%	0.04%	1	0	1	1	1
Scenario 3	-0.29	-0.9%	-4.9%	0.5%	0.1%	1	0	1	1	1

*EBITDA – Earnings before interest, tax, depreciation and amortisation

The base case scenario shows the number of financial measures underperforming to the Code thresholds as a point of comparison to the three scenarios analysed in this paper. For example, seven out of the 18 FPRs for Tier 1 CHPs reported an operating EBITDA margin below 8% while only one out of the five FPRs for Tier 2 CHPs reported an operating EBITDA margin below 3% in 2019-20.

In 2019-20 Tier 1 FPRs have a combined affordable housing rent revenue reduction of $2.4 million and $7.21 million in scenario 1 and scenario 2 respectively. The average affordable housing rent revenue reduction as a percentage of operating income is 0.4% in scenario 1 and 1.1% in scenario 2, both of which are not material. The number of financial measures underperforming to the Code thresholds is the same in scenario 1 and scenario 2. Both scenarios increase by one only the number of underperforming measures in operating EBITDA margin and interest cover ratio compared to the base case scenario.

In the highly unlikely scenario 3, Tier 1 FPRs have a combined affordable housing rent revenue reduction of $24.03 million, being 3.1% reduction in operating income in 2019-20. The average affordable housing rent revenue reduction as a percentage of operating income is 3.7%, which is also not material. 12 FPRs, five more than the base case scenario, underperform in operating EBITDA margin. Operating margin affects directly ICR which increased from three in the base case scenario to six the number of FPRs underperforming in this measure. Average performance of both measures remain above Code thresholds.

In all three scenarios net operating cash flow would be more affected than operating income for Tier 1 FPRs. Even though CHPs would be more affected in the generation of cash flows from operating activities, the ultimate cash balance would not be significantly affected. The number of FPRs underperforming to the Code thresholds increases by one only for working capital ratio in scenario 3 and remaining the same as in the base case scenario for amended quick ratio in all three scenarios. Average performance of liquidity ratios remains sound in all three scenarios. This is possible because Tier 1 FPRs have overall healthy cash balances and some of them have access to available and unused line of credits.

The aggregated Tier 1 FPRs would remain stable as the reduction in affordable housing rent revenue would have an immaterial financial impact on operating income and liquidity in all three scenarios in 2019-20. Average performance of operating margin ratios remain above threshold in scenario 3. Individual FPRs presenting a combined underperformance in measures related to operating performance, liquidity, cash flow, and ICR would be assessed on a per case basis on its own merits.

Tier 2 FPRs had a much lower impact in the main financial indicators and measures than Tier 1 FPRs in all three scenarios in 2019-20. In fact, three out of the five Tier 2 CHPs do not provide affordable housing and hence their financial indicators and thus those measures were not affected. The remaining two Tier 2 FPRs would be able to absorb potential rent revenue reductions from affordable housing in all three scenarios without increasing the number of financial measures underperforming to the Code thresholds from the base case scenario. The whole sample of Tier 2 FPRs would remain stable in all three scenarios in 2019-20.

Financial Impact in Forecast Year 2020-21

	Rent Revenue Reduction ($ Millions)	Avg % Reduction in Operating EBITDA	Avg % Reduction in Net Operating Cash Flow	Avg Rent Revenue Reduction as a % of Op Income	Avg Rent Revenue Reduction as a % of Net Assets	Number of financial measures underperforming to NRC thresholds				
						Operating EBITDA Margin	Working Capital Ratio	Amended Quick Ratio	Gearing Ratio	Interest Cover Ratio
Tier 1										
18 FPRs										
Base case	0.00	0.0%	0.0%	0.0%	0.0%	6	1	2	1	1
Scenario 1	-10.42	-13.9%	-20.1%	1.7%	0.5%	11	2	2	1	3
Scenario 2	-31.26	-41.7%	-60.2%	5.0%	1.5%	13	2	2	1	7
Scenario 3	-104.19	-139.0%	-200.6%	16.7%	5.0%	16	5	4	1	9
Tier 2										
5 FPRs										
Base case	0.00	0.0%	0.0%	0.0%	0.0%	1	0	0	1	1
Scenario 1	-0.20	-0.3%	-1.2%	0.2%	0.1%	1	0	0	1	1
Scenario 2	-0.60	-1.0%	-3.5%	0.6%	0.2%	1	0	0	1	1
Scenario 3	-2.01	-3.3%	-11.6%	2.1%	0.6%	1	0	0	1	1

In the base case scenario, the number of financial measures underperforming to the Code thresholds in 2020-21 is less than the number of financial measures underperforming in 2019-20 mainly for Tier 1 FPRs. This is a reflection of the overall growth this sub-sector is expecting in the short-term.

Tier 1 FPRs have a combined affordable housing rent revenue reduction of $10.42 million and $31.26 million, being 1.3% and 3.9% reduction on operating income in scenario 1 and 2 respectively in 2020-21. This financial impact is still not material. The average rent revenue reduction on operating income is 1.7% in scenario 1 and 5% in scenario 2. Two individual FPRs and four individual FPRs have a rent revenue reduction over operating income above 5% in scenario 1 and scenario 2 respectively.

Operating EBITDA and net operating cash flow are the most sensitive financial indicators in this analysis. A change in one variable, in this case affordable housing rent revenue, has a significant impact on the bottom line which contemplates all operating income minus all operating expenditure in the one period. Due to this sensitivity, operating EBITDA margin and therefore ICR are the financial measures most affected in this analysis for Tier 1 FPRs.

The number of FPRs with underperforming operating EBITDA margin increases from six in the base case scenario to 11 in scenario 1 and 13 in scenario 2. The number of FPRs with underperforming ICR increases from one in the base case scenario to three in scenario 1 and seven in scenario 2. Average performance of operating margin ratios remain above threshold in scenario 1 and below threshold but still positive in scenario 2. Two FPRs have negative margins in scenario 2. Average ICR remains above threshold in both scenarios.

The reduction in net operating cash flows is significant in scenario 1 and scenario 2. However, cash balances are not affected materially by the reduction in rent revenue. The number of FPRs with underperforming amended quick ratio remains the same in both scenarios as in the base case scenario while number of FPRs with underperforming working capital ratio increases by one in both scenarios. Incumbent ratios are slightly affected but the average performance of liquidity ratios remains sound in these two scenarios.

In the highly unlikely scenario 3, Tier 1 FPRs have a combined affordable housing rent revenue reduction of $104.19 million, being 12.9% reduction in operating income in 2020-21. The average affordable housing rent revenue reduction as a percentage of operating income is 16.7%. This level of reduction in affordable housing rent revenue is not only material, but

affects drastically the average percentage of reduction in operating EBITDA margin to -139% and the average percentage reduction in net operating cash flow ratio to -200.6% in 2020-21.

14 individual Tier 1 FPRs have a rent revenue reduction over operating income above 5% in scenario 3. The incumbent underperforming ratios deteriorate to a much higher degree and the number of FPRs with underperforming operating EBITDA margin and ICR increases considerably to 16 and nine respectively. Average performance of operating margin ratios is -31.9%. Nine individual FPRs have negative operating margins. Average ICR is above threshold.

Despite the fact operating performance is badly damaged by the loss of affordable housing rent revenue in scenario 3, liquidity ratios are impacted much more modestly in 2020-21. Five Tier 1 FPRs have underperforming working capital ratios, four more than the base case scenario. Similarly, four FPRs have underperforming amended quick ratios, two more than the base case scenario. Average performance of liquidity ratios remain above Code threshold in this scenario. As noted earlier, this is possible because Tier 1 FPRs have overall healthy cash balances and some of them have access to available and unused line of credits.

The aggregated Tier 1 FPRs would remain stable as the reduction in affordable housing rent revenue would have an immaterial financial impact on operating income and liquidity in scenario 1 and scenario 2 in 2020-21. Average performance of operating margin ratios remain above Code threshold in scenario 1 and below threshold but positive in scenario 2.

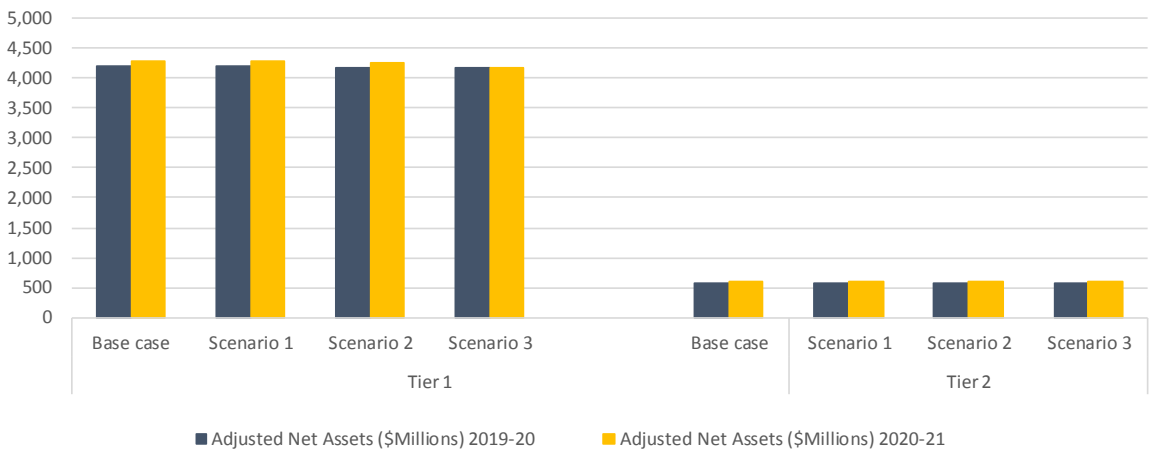
The aggregated Tier 1 FPRs have a material impact on operating income and overall operating performance in scenario 3 in 2020-21. The impact on liquidity is not material. The damage on operating performance is so significant that it could generate threats to short-term viability if any other variable, as explained in the assumptions section, does not change.

Individual FPRs presenting a combined underperformance in measures related to operating performance, liquidity, cash flow, and ICR would be assessed on a per case basis on its own merits.

Similar to 2019-20, Tier 2 FPRs are not materially affected by the reduction of affordable housing rent in any of the three scenarios analysed in 2020-21. The combined affordable housing rent revenue reduction is $0.20 million, $0.60 million, and $2.01 million in scenarios 1, 2, and 3 respectively. The average affordable housing rent revenue reduction as a percentage of operating income is 0.2% in scenario 1, 0.6% in scenario 2, and 2.1% in scenario 3; in all scenarios it is not material.

Cash balances and current assets remain sound as no liquidity ratios underperform in the base case scenario and any of the three scenarios analysed. Once again all Tier 2 FPRs would remain stable in all three scenarios in 2020-21.

The average rent revenue reduction as a percentage of net assets is not material in all scenarios in 2019-20 and 2020-21 due to the healthy condition of balance sheets for Tier 1 & 2 FPRs. The average impact in net assets is 5% or less for Tier 1 FPRs in all scenarios across the two forecast years. Likewise, the average impact in net assets is less than 1% for Tier 2 FPRs in all scenarios across the two forecast years.



Capital structure has minimal impact measured through gearing ratio and adjusted net assets. Average gearing ratio increases by 2.1% in scenario 3, the worst case scenario, in 2020-21 for Tier 1 FPRs. The number of underperforming gearing ratios remain always the same as it does in the base case in all scenarios across the two forecast years.

Adjusted net assets is $4.16 billion in 2019-20, a 0.6% decrease to the balance in the base case scenario and $4.18 billion in 2020-21, a 2.4% decrease to the balance in the base case scenario for Tier 1 FPRs.

CHPs have strong balance sheets. This means they have robust total asset and net asset positions that allows them to elaborate strategies and/or mitigate financial risks from perilous financial performances created by the loss of rent revenue in affordable housing due to COVID-19 and to remain viable or solvent in the foreseeable future.

IMMEDIATE FINANCIAL VIABILITY IMPACT

In anecdotal evidence, most of the CHPs queried about immediate financial impact due to COVID-19 have indicated that they do not expect a material rent revenue reduction or rent arrears that could threaten viability in the forecast year 2019-20.

CHPs are consistently reporting they are proactively monitoring the potential financial impact of COVID-19 and putting in processes to mitigate losses. Reponses include regular scenario testing of various level arrears, daily monitoring of Centrelink cancellations, and increased emphasis on rental collections.

CHPs are also implementing measures and assumptions that will help them minimise financial impact. One CHP with a significant proportion of affordable housing in their portfolio is cutting rent in half immediately and expecting tenants to get support from Centrelink where the CHP retains a percentage of income. Another CHP has paused rent reviews.

CHPs have further explained that they are managing tenants unable to continue paying rent on a case by case basis and with each case assessed determined on its own merits.

Several CHPs report that their income from affordable housing has remained stable largely as a result of government initiatives designed to minimise the economic impact of COVID-19. However, the situation could change significantly when these programs are wound back.

While not factored into this analysis many CHPs stated in the short run that while they expected a decline in rental income, this would be offset by a reduction in corporate overheads, such as reduced expenditure in travel or training, and non-urgent maintenance due to restrictions on inspecting properties.

For the next six to 18 months, concern was expressed over social housing tenants on statutory income erroneously thinking they had a rent holiday as well as a possible freeze on rental increases in coming years.

CHPs who expressed the greatest concern over the financial impact of COVID-19 tend to be those who historically have lower levels of profitability. These providers believe COVID-19 could exacerbate existing financial stresses into more serious issues, whereas providers with healthier levels of financial performance are in a better situation to absorb any impact.

CHPs also expressed that in this constantly changing environment caused by COVID-19 it is premature to budget the financial impact in 2020-21.

The Office of the Registrar is not the only one anticipating analysis of the financial impact of COVID-19 on CHPs. Some CHPs have refinanced their debt with the National Housing Finance and Investment Corporation (NHFIC), providing ten-year interest only loans with repayment of principal at the end of the loan period.

NHFIC has been in contact with relevant CHPs to monitor the impact of COVID-19.

CONCLUSION

23 FPRs used in this sensitivity analysis have different proportions of affordable housing within their portfolios that directly affect the financial impact of rent revenue reduction. 18 FPRs belong to Tier 1 CHPs and five FPRs belong to Tier 2 CHPs.

The aggregated Tier 1 FPRs would remain stable as the reduction in affordable housing rent revenue would have an immaterial financial impact on operating income and liquidity in all three scenarios in 2019-20. Average performance of operating margin ratios and liquidity ratios remain above the Code thresholds in all scenarios.

The aggregated Tier 1 FPRs would remain stable as the reduction in affordable housing rent revenue would have an immaterial financial impact on operating income and liquidity in scenario 1 and scenario 2 in 2020-21. Average performance of operating margin ratios remain above the Code thresholds in scenario 1 and below the Code thresholds but still positive in scenario 2.

The aggregated Tier 1 FPRs have a material impact on operating income and overall operating performance in 2020-21. The impact on liquidity is not material. The damage in operating performance is so significant that it could generate threats to short-term viability if any other variable, as explained in the assumptions section, does not change.

The aggregated Tier 2 FPRs would remain stable in all three scenarios in 2019-20 and 2020-21. The overall financial impact is not material across the two forecast years.

Individual FPRs presenting a combined underperformance in measures related to operating performance, liquidity, cash flow, and ICR would be assessed on a per case basis on its own merits. The degree of the financial impact on each CHP depends on the proportion of affordable housing to the overall housing and the size of the provider.

CHPs have strong balance sheets. This means they have robust total asset and net asset positions that allows them to develop strategies and/or mitigate financial risks from perilous financial performances created by the loss of rent revenue in affordable housing due to COVID-19 and to remain viable or solvent for the foreseeable future.

Most CHPs expressed little or no concern about the immediate financial impact of reduced rent revenue or rent arrears in 2019-20.

After completing the sensitivity analysis in addressing the financial impact derived from the partial or total loss of affordable housing rent revenue due to COVID-19, the results from the scenario analysis indicate that the aggregated 23 FPRs would have a short-term impact in operating performance and viability but would remain solvent in the foreseeable future.

NSW Registrar of Community Housing
Locked Bag 4001, Ashfield BC 1800
P: 1800 330 940 F: (02) 8741 2522
E: registrar@facs.nsw.gov.au
W: www.rch.nsw.gov.au