DTP VIEWS

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Value for Money could make mergers more common

– Sam McGrady, Director, DTP

In a previous blog I cautioned that the regulator's new Value for Money Standard for the social housing sector could have unintended consequences – and that by their nature these are difficult to predict. Well a consequence is certainly starting to emerge – although to be fair to the regulator its intentions were not exactly hidden. Still, the reaction probably wasn't expected.

The standard places a requirement on Registered Providers (RPs) to give, "regular and appropriate consideration by the board of potential value for money gains – this must include full consideration of costs and benefits of alternative commercial, organisational and delivery structures'. It doesn't take much reading between the lines to see that this means mergers should be given serious air time by boards.

Given the first reporting against the standard isn't due until autumn we may have to wait a while to see how this might play out. But already some of the smaller providers I've been talking to are worried. Their concern is that they could be bounced into mergers against their will. Often faced with higher operating costs – now publicly available for all to see – there could be pressure on them to consider joining forces with a larger provider as the answer to all their problems.

My view is some of the smaller housing associations might be worrying unnecessarily. And there are several reasons why.

The crucial thing to remember here is the government doesn't simply want to see mergers for mergers' sake. It wants to see fewer, larger RPs because it believes this will improve operational efficiency. And it thinks improved operational efficiency will free up more resources for development. More homes is the aim, how we get there is up for grabs.

Firstly, all RPs are independent and can't be forced to merge. Concerned smaller providers should remember this – although it's true pressure can be applied.

I think the key defence against unwanted mergers may come from the government's own arguments about efficiency. Put simply: merging a small RP of say less than 1,000 properties into a larger organisation probably won't deliver significant cost savings for either party. And when you remember that providers with less than 1,000 homes account for just 5% of all social housing provision, it isn't going to have a big impact on the government's overall aim to increase the amount of development.

It can be argued that the sector would be better off if merger efforts were focused on medium and larger organisations. Here, the benefits are still there for the taking: staff/management reductions, procurement wins from economies of scale and cheaper office and accommodation, lower overheads including HR, finance and legal. We've worked with a number of RPs in recent years which have gone down this route and are able to demonstrate very significant, quantifiable savings in the first few years, alongside increased development capacity. The key is to make sure you set targets for efficiencies and measure how you are performing against these over an agreed period of time. And if you go off course, get back on quickly!

Of course, other options are available to smaller providers – without necessarily going down the full merger route.

They may be able to tap into some of the benefits enjoyed by larger organisations by nature of their size. For example, a small provider might not be able to justify having its own legal team, but it could procure the services of a lawyer from a larger provider which can. This is likely to be cheaper than hiring a lawyer from the commercial sector, plus it keeps things 'in-sector'. Cost sharing vehicles to pay for services such as repairs and gas servicing are also an option, and there are some good examples of these working well. Collaboration and partnerships may therefore be the best route to improved efficiency for some.

Reviewing current organisational structures could also offer some providers another reasonable defence against merger. Are those subsidiaries you set up to a few years ago still the best way to deliver your objectives? Are they largely creating another layer of management and bureaucracy? Could your organisation achieve cost savings from a simpler, more flatter structure? Probably. It's certainly worth looking into and taking some expert advice.

Ultimately, the regulator is not fixated on mergers but wants to see a continued emphasis on efficiency. Whatever works should be the approach.

The Value for Money Standard should itself help with this. It has been broadly welcomed and offers a clearer and simpler system of reporting. No system of regulation will ever be perfect, however. And I certainly can't guarantee there will be no further unintended consequences in the future. We await the first reporting of figures in the autumn with anticipation.

- *For more insight into the sector's response to the new Value for Money Standard read the first edition of DTP Exchange, our twice yearly thought leadership report on the social housing sector. DTP Exchange features interviews with 19 chief executives and sector leaders as well as expert commentary from a housing lawyer on the key issues facing RPs right now.*