Appendix 3
Definitions of key ratios and Regulation Office review thresholds

Set out below are the definitions of the key ratios used by the Regulation Office in carrying out its financial assessment. The Regulation Office has established its own review thresholds for each of these measures which are used as part of the overall assessment. These review thresholds may vary over time and are not intended to be targets which AHBs must achieve. Each individual AHB should consider what the appropriate threshold levels are for the organisation which should be based on its overall risk appetite.

a) EBITDA

EBITDA stands for Earnings Before Interest Tax Depreciation and Amortisation. This is a standard measure of revenue performance which seeks to eliminate non-cash items (depreciation and capital grant amortisation), remove funding costs and adjust for transfers to or from reserves to give a comparable measure between organisations.

EBITDA is calculated as:

Operating surplus + depreciation – capital grant amortisation

Where Operating Surplus includes any transfers to or from a major repairs reserve or sinking fund these must also be added back or deducted from Operating Surplus to arrive at EBITDA.

Capital grant amortisation refers the amortisation of CLSS, CAS and other capital funding where included in Turnover.

b) EBITDA margin

EBITDA margin is calculated as follows:

$$\frac{\text{EBITDA}}{\text{(Turnover – capital grant amortisation)}}$$

Review threshold of 20% for the first four years rising to 30% from year five as new developments come into management.

c) EBITDA Interest Cover

This is a standard measure of the ability of the organisation to meet interest costs. It is calculated as:

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EBITDA
(Interest payable – interest receivable)

Whilst AHBs currently have very low external borrowing and hence pay little interest this ratio will be very high but as borrowing increases to fund development the ratio will fall. We have set a review threshold of 120% for this ratio.

d) Debt service cover ratio

This is a standard measure of the ability of the organisation to meet interest costs. It is calculated as:

EBITDA
(Interest paid + loan capital repayments– interest received)

As with interest cover this ratio will fall as external borrowing increases and we have set a review threshold of 110%.

e) Gearing

This is a standard measure of the proportion of the ratio of net borrowing to the historic cost of housing properties. It is calculated as:

(Private finance loans + CALF- cash)
Historic cost of housing properties

Where:

Historic cost of housing properties = the gross cost of housing land and buildings in the Balance Sheet before any accumulated depreciation

This ratio will normally increase as external borrowing increases dependent on grant levels. We have set a review threshold of 60% for this measure.

f) External debt per unit

This is a straightforward measure calculated as:

(Private finance loans + CALF)
Units owned

The measure allows monitoring of the level of funding in relation to the size of the organisation.

g) Cash from operations

This is defined as:

EBITDA

(Turnover – capital grant amortisation)

This is a measure of the overall ability of the organisation to generate a positive cashflow with a review threshold of at least 10% and a minimum break-even of 0%.

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h) Liquidity (Quick ratio)

This is defined as:

$$\frac{\text{(Debtors + cash + secured undrawn loan facilities)}}{\text{Current liabilities}}$$

This is a measure of the ability to meet short term liabilities from cash or cash equivalents. The review threshold for this 1.5:1.

i) Other indicators

In addition to the above key indicators we will review information in the following areas:

- Voids (occupancy level)
- Asset cover (ratio of loans to security valuation) and available security for future borrowing
- Ability to meet and maintain stock to the required standard
- Appropriate business planning and sensitivity testing of the plan to adverse impacts
- Risk assessment and mitigation

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