Group Finance Director's review

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Nish Malde
Group Finance Director

Introduction

Whilst COVID-19 had a disruptive effect on the first half of the year operationally, the underlying strength of the housing market and demand for the quality homes built by the Group held sway over the wider economic uncertainties. Following what was a period of record sales activity, in the second half of the year, and with the extension of the fiscal stimuli provided by the Government, the land market heated up. Demand for land and residential property in the South and South East, the areas in which the Group operates, continues to remain strong.

As a result, the Group has delivered on its commitment to reduce net debt and will continue to target further reductions. We have also successfully grown our asset management, partnership housing and housebuilding activities. Although the Group's share price continues to trade at a significant discount to its published net EPRA value per ordinary share, the focus on positive cash generation, when set alongside our operational achievements, will continue to drive value in the coming financial year.

Net debt and borrowings

The Board's key strategic objective was to reduce the Group's net debt. I am therefore pleased to report that the Group's net debt has reduced by £30.1m, some 20.3%, from £148.2m (30 September 2020) to £118.1m at the financial year end. This represents net gearing of 64.5% (30 September 2020: 85.7%) and net gearing based on EPRA net assets of £246.4m of 47.9% (30 September 2020: 63.0%).

Subsequent to the financial year end, there has been further debt reduction arising as a result of the advanced receipt of £8.3m from the contract for the forward sale of 161 homes in Poole.

Changes in performance measures for EPRA

In October 2019, the European Public Real Estate Association (EPRA) published new Best Practice Recommendations for financial disclosures by listed real estate companies. The Group supports standardised reporting to improve the quality and comparability of information for investors. The BPR introduced two new measures of net asset value: EPRA net tangible assets (NTA) and net disposal value (NDV). We have adopted these guidelines in the year ended 30 September 2021 and consider EPRA NTA to be the most relevant measure for our business. EPRA NTA will now be our primary measure of net asset value, replacing our previously reported EPRA net assets and EPRA net assets per share measures. We have also restated the EPRA NAV to EPRA NTA as of 30 September 2020 for comparative purposes, including the prior period adjustment as disclosed in Note 41.

£118.1m
Net debt
2020: £148.2m

Balance sheet

The Group's net assets have increased to £183.0m at 30 September 2021 (30 September 2020: £173.0m), mostly due to the retained profit after tax that the Group has reported for this financial year.

The EPRA NTA at 30 September 2021 increased to £246.4m (30 September 2020: £235.2m). Net asset value per ordinary share increased to 80.10p (30 September 2020: 76.31p) and EPRA NTA per ordinary share was 107.84p per share (30 September 2020: 103.75p). A reconciliation of EPRA tangible net asset value is on page 45.

The Board is required to assess the fair value of the Group's sites held in current assets, when determining EPRA NTA. For undeveloped sites (both owned and controlled by way of options), a residual land valuation is carried out to determine the expected value of the site with planning consent. The valuation is then discounted by a factor of between 0% to 90% to reflect the probability of achieving planning permission.

There is not a ready market for sites where construction has commenced. The Directors have, therefore, assumed that fair value equates to the carrying value for such sites unless the site is forecast to make a gross margin of more than 16% (an industry standard benchmark), in which case a fair value adjustment is made to reflect the residual land value uplift.

The Group transferred further residential and commercial property from assets held for sale as it is intended that these will be held for long-term purposes. In addition, 18 residential properties at Wilton Park, Beaconsfield have been transferred from investment properties to inventories, as these properties are being demolished to make way for the construction of a link road, which the Group is required to construct under a legal agreement with the local authority. The balance of investment properties, amounting to £36.0m (2020: £43.5m), principally comprises the remaining existing residential properties at Wilton Park. In accordance with IFRS 16 Leases, the lease of our head office in Beaconsfield and a car have been capitalised and classified as right-of-use assets at £0.9m (2020: £1.2m), with a corresponding lease liability of £0.9m (2020: £1.2m) at the year-end.

Investment in joint ventures consists of the Group's four joint ventures, the most significant of which is our investment at Cheshunt, held through Cheshunt Lakeside Developments Limited (CLDL), which amounted to £4.2m (30 September 2020: £6.3m). In addition, there were amounts due from joint ventures, held as a non-current asset, being £32.7m (30 September 2020: £28.6m). Similarly, other receivables due after more than one year, of £22.0m (30 September 2020: £20.7m), represents the amount due from our joint venture partner in CLDL, which is secured by way of a charge over their share of profits from the development.

Inventories have reduced to £163.9m (30 September 2020: £173.6m), due to land sales and sales of residential property. Trade and other receivables due within one year have increased to £116.9m (30 September 2020: £60.9m), principally due to a significant increase in management fees accrued from our asset management activities. These fees will be received as the relevant sites are monetised.

As explained above, net debt at the year end was £118.1m (2020: £148.2m). Gross borrowings were £130.2m (30 September 2020: £163.9m) with cash balances of £12.1m (30 September 2020: £15.7m).

During the year, the Group repaid loan facilities with Homes England, which financed our development at Chapel Riverside in Southampton, and also repaid facilities from mainstream lenders which financed some of our land and housebuilding projects.

At the year end, the Group had drawn down £33.9m of our £65.0m revolving credit facility with HSBC (30 September 2020: £42.4m), leaving headroom for future housebuilding projects of £30.6m (30 September 2020: £22.6m). This facility expires in March 2023.

At the year end, the accrued liability to holders of Zero Dividend Preference (ZDP) shares was £32.0m (30 September 2020: £30.2m). The accrued liability is due to be repaid to the holders of ZDP shares in April 2024, unless extended with the agreement of the ZDP holders, before that date.

Operational performance

The Group's revenue for the year to 30 September 2021 has increased sharply to a record £181.7m (30 September 2020: £124.0m), boosted by the sales of 216 private homes (30 September 2020: 96) (excluding those via joint ventures) and bulk sales to BtR operators. The average selling price increased to £262,000 (30 September 2020: £240,000).

The Group's weekly net reservation rate per active sales outlet, excluding joint ventures, was 1.09 for the year (30 September 2020: 0.65), which underlined the strength of the market in the areas in which Inland Homes operates. Purchasers of 45% (30 September 2020: 56%) of our new homes made use of the Help to Buy scheme, excluding joint ventures. Our forward order book of homes reserved and exchanged as at the year end amounted to £33.4m (30 September 2020: £37.5m).

The total number of plots within our land bank decreased marginally, after the sale of 601[1] residential plots by the Group, including plots from within our asset management business.

The revenue from our partnership housing activity was £60.3m (30 September 2020: £51.8m) from contracts across six sites. As at 30 September 2021, the forward order book for partnership housing contract income was £164.7m (30 September 2020: £105.8m), with two new contracts secured during the year for total revenue of £131.3m. The Group's focus will continue to be in growing the partnership housing activity as it

£246.4m

EPRA net tangible assets

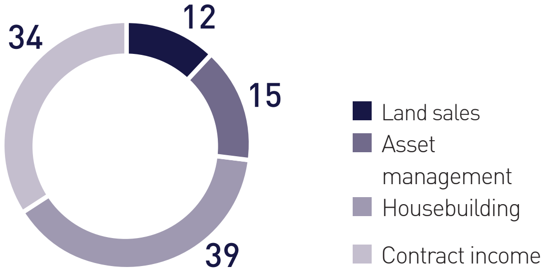
2020: £235.2m

107.84p

EPRA net tangible assets per ordinary share

2020: 103.75p

Revenue by segment (%)



[1] Includes plots within the asset management division owned by third parties.

generally secures a land sale together with a forward income stream, providing a good balance to the Group's business model.

The Group's asset management division, which acts on behalf of property investors to procure sites and provide planning and management services, has six live projects (30 September 2020: six projects) in Greater London. During the financial year, the Group earned management fees of £27.8m (30 September 2020: £24.4m) from these contracts. The transactions are structured so that they require significantly reduced investment and working capital from Inland Homes and are also, generally, non-recourse to the Group. Once these sites receive planning consent, they are sold to Build to Rent (BtR) or other purchasers, which can often lead to a partnership housing contract for the Group.

Other revenue of £1.8m (30 September 2020: £2.3m) includes letting income from investment properties and short-term rents from brownfield sites being processed through the planning system.

Gross profit increased to £32.0m (30 September 2020: £22.0m) because of higher profits from land sales, management fees and private homes sold by the Group.

The gross profit margins of the Group's partnership housing and housebuilding businesses are currently unsatisfactory. As previously reported with the Interim Results for the six-months ended 31 March 2021, the Group became aware of approximately £3.5m of unforeseen additional costs relating to one housebuilding site and a single partnership housing contract. These costs were somewhat offset by £0.4m of additional revenue from higher selling prices achieved from the Group's housebuilding sites.

In common with many in the industry, the Group has also experienced mid-single digit cost inflation, some of which has been mitigated by higher than forecast selling price of its new homes. There are, however, recent signs that some of the more pronounced price rises over recent months are beginning to subside. The industry has also witnessed some ongoing constraints in the supply chain and intermittent labour shortages. These factors have also impacted gross margins during the year and will continue to have an impact in the current financial year.

The Group wrote off £0.5m work-in-progress relating to aborted land transactions (30 September 2020: £2.1m) and made provisions for £3.4m where future cost overruns are envisaged following detailed project reviews (30 September 2020: £0.1m). At 30 September 2021, the Group has contingency provisions of £3.1m (30 September 2020: £4.0m).

As a result, the Group has undertaken a number of measures to improve both operational efficiency and commercial delivery, with the objective of improving margins in the partnership housing and housebuilding businesses. The Group has moved to further standardise drawings and specifications in order to assist onsite construction efficiency and to deliver costs savings through design evolution and centralised procurement deals. Improvements have also been made to the Group's IT system, which has improved transparency and accountability in the project evaluation process. As a result of the steps taken and the planned ongoing work in this area, the Board currently expects to see some margin improvement in the coming financial year.

Consequently, gross margin reduced to 17.6% (30 September 2020: 17.7%) and operating margin increased to 11.6% (30 September 2020: 9.5%). A detailed analysis by operating segment is shown in Note 10 to the Financial Statements on pages 119–123.

Administrative expenses have significantly decreased to £7.5m (30 September 2020: £12.6m), as the Group rationalised its operations into the six operating businesses. Administrative overheads comprise salary costs for the main Board (as disclosed in the Remuneration Report on pages 78-82) and non-operational staff totalling £6.1m (30 September 2020: £8.7m), central overhead of £0.8m (30 September 2020: £4.4m) and depreciation of £1.1m (30 September 2020: £1.3m).

Net finance costs

Finance costs of £9.3m (30 September 2020: £9.5m) comprised principally of bank and other loan interest, amortisation of arrangement fees and exit fees, non-utilisation fees and interest rolled up on the Zero Dividend Preference shares (ZDPs). Finance income of £1.5m (30 September 2020: £1.1m) includes interest from joint ventures and associates, other interest receivable and notional interest income on long-term receivables. Finance costs were relatively high until near the end of the financial year, when the Group's borrowings fell as a result of the significant number of land and private home sales affected. Interest on development funding is capitalised as required by IAS 23. No interest was capitalised during the year (30 September 2020: £0.8m).

Taxation

The Group is domiciled in the United Kingdom and does not make use of any tax structure that is not domiciled in the United Kingdom.

The total tax charge of £3.6m combines a current taxation charge of £4.3m and a deferred tax credit of £0.7m and represents an effective rate of 27.3% of the profit before tax. The current corporation tax rate is 19% and the difference between the expected tax charge and the actual tax charge is mainly due to the interest accrued on the ZDPs, which are disallowed for tax purposes.

Prior year adjustment

The Group has a prior year adjustment in respect of deferred contingent consideration payments for the site at Wilton Park, Beaconsfield not being recognised in prior periods.

Site assembly occurred in 2010 when the Group entered into two land option contracts which committed to deferred contingent consideration payments on grant of a planning permission for the site over a period from the date of the planning consent. The two land option contracts also contained standard overage clauses which are triggered in certain future circumstances based on the actual delivery of housing for the site.

The Group did not recognise in 2019 the deferred contingent consideration payments on the grant of a planning permission. The liability of £6.0m was unconditionally triggered in September 2019 of which, £4.8m remains unpaid at 30 September 2021.

Earnings per share and dividends

Basic earnings per share increased to 4.21p per ordinary share (30 September 2020: 0.65p per ordinary share), reflecting the Group's improved retained profit after tax in this financial year.

Going Concern

In preparing the forecasts, the Directors have considered the continued adoption of stringent cash management procedures, market disruptions already brought about by COVID-19, the possibility of future disruption in the Going Concern period, which could potentially be caused by COVID-19, and other risks and uncertainties, including credit risk and liquidity risk, the present and possible future economic climate, the current and possible future demand for land with planning consent and the state of the housing market in the geographic areas where the Group operates.

The Directors have performed detailed sensitivity analyses to test the Group's future liquidity and banking covenant compliance based on several scenarios.

The Directors have a reasonable expectation that the Group and parent Company have adequate resources to continue in operational existence for the foreseeable future. The Directors therefore consider it appropriate to prepare the Financial Statements on the Going Concern basis. Further details can be found in Note 2 on pages 102–103.

Outlook

We ended this financial year having achieved a significant reduction in the Group's net debt to £118.1m, whilst holding a land bank of 10,055 plots. We are well positioned to serve the private housebuilding and partnership housing sectors with land, asset management and construction services over the short, medium and long term.

Demand for housing in our market of the South and South East of England continues apace and in the Budget on 27 October 2021, the Government announced its desire to utilise Britain's brownfield land to help address the housing crisis, investing £1.8bn to deliver 160,000 new homes. Brownfield land is at the heart of Inland Homes' business and the Group is accordingly well placed to benefit from the Government's stated intention to unlock more brownfield sites.

The focus for the coming financial year continues to be the reduction in Group net debt and the improvement of margins in the partnership housing and housebuilding businesses. Externally, our award-winning new homes continue to delight customers and investors alike. The Group's land pipeline of brownfield and strategic sites located in the South and South East of England leaves the Group well placed to make further progress in the coming year.

Nish Malde
Group Finance Director
31 January 2022

	Previously reported measures		New measures	
	EPRA net assets £m	EPRA triple net asset value £m	EPRA NTA £m	EPRA NDV £m
At 30 September 2021				
Net assets attributable to equity shareholders	**183.0**	**183.0**	**183.0**	**183.0**
Adjustments for:				
Revaluation of projects	**61.8**	**61.8**	**61.8**	**61.8**
Deferred tax on investment property revaluation	**1.7**	**1.7**	**1.7**	**-**
Other intangible assets	**-**	**-**	**(0.1)**	**-**
Adjustment for:				
Deferred tax on investment property revaluation	**-**	**(1.7)**	**–**	**–**
Deferred tax on project revaluation	**-**	**(15.4)**	**–**	**–**
EPRA net asset value used in per share calculation	**246.5**	**229.3**	**246.4**	**244.8**
EPRA net asset value (pence per share)	**107.88**	**100.38**	**107.84**	**107.14**

	Previously reported measures		New measures	
	EPRA net assets £m	EPRA triple net asset value £m	EPRA NTA £m	EPRA NDV £m
At 30 September 2020				
Net assets attributable to equity shareholders	173.0	173.0	173.0	173.0
Adjustments for:				
Revaluation of projects	59.8	59.8	59.8	59.8
Deferred tax on investment property revaluation	2.6	2.6	2.6	-
Other intangible assets	-	-	(0.2)	-
Adjustment for:				
Deferred tax on investment property revaluation	-	(2.6)	–	–
Deferred tax on project revaluation	-	(11.4)	–	–
EPRA net asset value used in per share calculation	235.4	221.4	235.2	232.8
EPRA net asset value (pence per share)	103.84	97.66	103.75	102.69