Property Investment Strategy – Risk Analysis

The Property Investment Strategy risks are detailed below. Each risk is first assessed **gross** (without existing controls in place) and then re-assessed following the identification of key controls to give the **net** score. Each risk is also given a **target** score, which is the desired rating for the risk. The overall **rating** (**R**) is derived by multiplying the **likelihood** (**L**) and the **impact (I)**.

Net Risk Ratings

Likelihood		Minimal (1)	Minor (2)	Moderate (3)	Major (4)	Critical (5)
	Very Likely (5)					
	Likely (4)					
	Possible (3)		**9b**	**12**		
	Unlikely (2)		**9d**	**4,9a,9c,9e**	**1**	
	Very Unlikely (1)		**3**	**7**	**2a**	**2b,5,6,8,10,11**

Impact

Risk Factors	Potential Effect	Gross Likelihood	Gross Impact	Gross Rating	Internal Controls	Net Likelihood	Net Impact	Net Rating	Target Likelihood	Target Impact	Target Rating
Property Investment Strategy Lead Officers: **Adrian Rowbotham & Detlev Munster**											
1) Downturn in property market	• Poor Return on Investment (ROI) on selling/rental	3	5	15	• Contracts to have rent review, break clauses etc. • Investments are credit secure and can be retained through any market downturn. • No requirement by SDC to liquidate investments in medium term. • No requirement from SDC to minimise or contain reported mark to market variability.	2	4	8	2	4	8

Risk Factors	Potential Effect	Gross Likelihood	Gross Impact	Gross Rating	Internal Controls	Net Likelihood	Net Impact	Net Rating	Target Likelihood	Target Impact	Target Rating
2) a. Poor quality construction/management	• Repairs • Defects • remedial work • customer dissatisfaction • loss of reputation • legal action • additional costs not built into financial plan	1	5	5	• Robust contracting process. • Pre-purchase surveys. • High quality spec. • Quality assurance clauses. • Warranties. • Procurement processes. • Clauses for liquidated damages. • Build relationships with contractors - understand their quality ethos. • Do not work with contractors who have a record issue or no track record.	1	4	4	1	4	4

Risk Factors	Potential Effect	Gross Likelihood	Gross Impact	Gross Rating	Internal Controls	Net Likelihood	Net Impact	Net Rating	Target Likelihood	Target Impact	Target Rating
					• Ensure contractor has sufficient covenant to stand behind their commitments. • Property Investment Strategy Maintenance Reserve.						
b. Poor quality construction/management	• Risks to personal health and safety - defects, gas, electricity, legionella, etc.	2	5	10	• Surveys; risk assessment techniques; CDM (Construction, Design & Mgt Regs); using registered suppliers and installers.	1	5	5	1	5	5
3) Possibility of challenge re: unlawful subsidy	• Legal challenge to Quercus 7.	2	2	4	• Full cost recovery.	1	2	2	1	2	2

Risk Factors	Potential Effect	Gross Likelihood	Gross Impact	Gross Rating	Internal Controls	Net Likelihood	Net Impact	Net Rating	Target Likelihood	Target Impact	Target Rating
					• Loans obtained at commercial lending rates. • Charging Directors and others' time to the Company. • Legal due diligence pre contractual commitment.						
4) Inability to attract and retain suitable purchasers/tenants.	• Poor ROI • void periods • loss of rental income	3	4	12	• Demand for residential property remains high. • Taking up references. • Early engagement with potential buyers/tenants. • Quality product to attract. purchasers/tenants. • Property Investment Strategy	2	3	6	2	3	6

Risk Factors	Potential Effect	Gross Likelihood	Gross Impact	Gross Rating	Internal Controls	Net Likelihood	Net Impact	Net Rating	Target Likelihood	Target Impact	Target Rating
					Maintenance Reserve to support downturn in market for tenants i.e. finance voids or rent shortfalls.						
5) Failure to fully assess sites and conditions	• Defects • remedial action • costs • failure to attract purchasers/tenants. • void periods • poor ROI	2	5	10	• Robust appraisals and surveys to be undertaken before progressing. • Pre-application planning advice. • Knowledge of location/market. • Extensive due diligence process.	1	5	5	1	5	5
6) Insufficient resources, capacity, skills to plan and manage projects.	• Inability to close deals as insufficient due diligence • Loss of reputation	3	5	15	• Procurement of specialist resources not available in-house. • Appointment of staff with	1	5	5	1	5	5

Risk Factors	Potential Effect	Gross Likelihood	Gross Impact	Gross Rating	Internal Controls	Net Likelihood	Net Impact	Net Rating	Target Likelihood	Target Impact	Target Rating
					adequate skills for purpose.						
7) Increase in voids/and void turn-around time/re-let times	• Income from rent is reduced and cash flow compromised	3	3	9	• Employment of experienced agents to manage lettings. • Sale of property an option. • Reconsideration of operating model. • Property Investment Strategy Maintenance Reserve to support downturn in market for tenants i.e. finance voids or rent shortfalls.	1	3	3	1	3	3

Risk Factors	Potential Effect	Gross Likelihood	Gross Impact	Gross Rating	Internal Controls	Net Likelihood	Net Impact	Net Rating	Target Likelihood	Target Impact	Target Rating
8) Purchase not supported by red book valuation	• Unable to secure purchase	4	5	20	• Red book valuation obtained prior to offer.	1	5	5	1	5	5
9) a. Financial risk: properties not re-let	• Rents not achieved. • Reduced income - •	3	4	12	• Invest in areas with high demand.	2	3	6	2	3	6
b. Financial risk: tenant default on rents	• Rents not achieved. • Reduced income	3	4	12	• Careful vetting of tenants pre-contract. • Limit exposure to an individual tenant. • Tight T&Cs in lease agreements. • Prompt chasing of rent arrears.	3	2	6	3	2	6
c. Financial risk: property market falls	• Values reduce. • Reduced income	2	3	6	• Diversified portfolio.	2	3	6	2	3	6

Risk Factors	Potential Effect	Gross Likelihood	Gross Impact	Gross Rating	Internal Controls	Net Likelihood	Net Impact	Net Rating	Target Likelihood	Target Impact	Target Rating
					• Actively assess market value. • Preparedness to sell if exposures are increasing.						
d. Financial risk: higher operational costs	• Reduced net income	2	2	4	• Tight budget and cost control. • Adopt corresponding terms in lease and agency agreements.	2	2	4	2	2	4
e. Financial risk: defects	• Reduced let ability. • Reduced income	2	4	8	• Conduct regular planned maintenance work and periodic inspections.	2	3	6	2	3	6
10) Failure to comply with taxation issues, Corporation tax and VAT.	• Legal challenges	2	5	10	• Internal and/or external advice sought in relation	1	5	5	1	5	5

Risk Factors	Potential Effect	Gross Likelihood	Gross Impact	Gross Rating	Internal Controls	Net Likelihood	Net Impact	Net Rating	Target Likelihood	Target Impact	Target Rating
					to taxation to ensure compliance.						
11) Poor management of property	• Risk to tenants • Health and Safety • Defects, gas, electricity etc.	2	5	10	• Engage experienced and qualified management agents. • Staff to keep abreast of statutory requirements. • Appropriate DMS and compliance regimes in place.	1	5	5	1	5	5
12) Political change – local or national	• Changes in policy and/or legislation affecting business model. • Increased financial burden placed which cannot be recouped from service charges.	3	5	15	• Maintenance provisions are held. • Where possible, tenants required to ensure upkeep and compliance.	3	3	9	3	3	9

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	• Changes to building standards resulting in uncosted refurbishments. Reputational damage.				• Lease agreements are carefully structured. • Maintain overwatch of political/policy changes as a result of local or national political change.						