An alternative investment in built social housing

Dear Shareholder,

Over recent months we have completed the investment of the equity and the first two debt tranches of CSH. We have also made good progress in investing part of the equity of CSHC, whilst continuing to build a nationally based, diversified portfolio.

We have recently undertaken a number of shareholder meetings and conference calls with both existing shareholders and non-holders of CSH and CSHC to update on our progress. These meetings have also reflected on the recent RNS announcement in relation to First Priority Housing Association, which has understandably raised some concerns. We thought it would be helpful to provide an update from these meetings as part of a broader commentary on our progress to date.

By way of background, CSH was launched in November 2016 as the first pure-play social housing REIT in the UK. We raised £350m through an over-subscribed IPO, to invest in properties in England and Wales. Then in November 2017, we raised a further £302m by way of a C Share, the proceeds of which we are investing at present.

Our mandate is to acquire built properties, fully tenanted and income-generating. We don't take development risk nor do we undertake any forward funding.

We implement our own new institutional-quality lease at the point of acquisition and these leases are prepared by leading sector-specialist lawyers, with whom we have long-term arrangements in place. We believe this approach enables us to achieve greater uniformity across the sector and ensures our portfolio benefits from the high levels of protection these leases afford us, on terms and tenure that are viable to all parties.

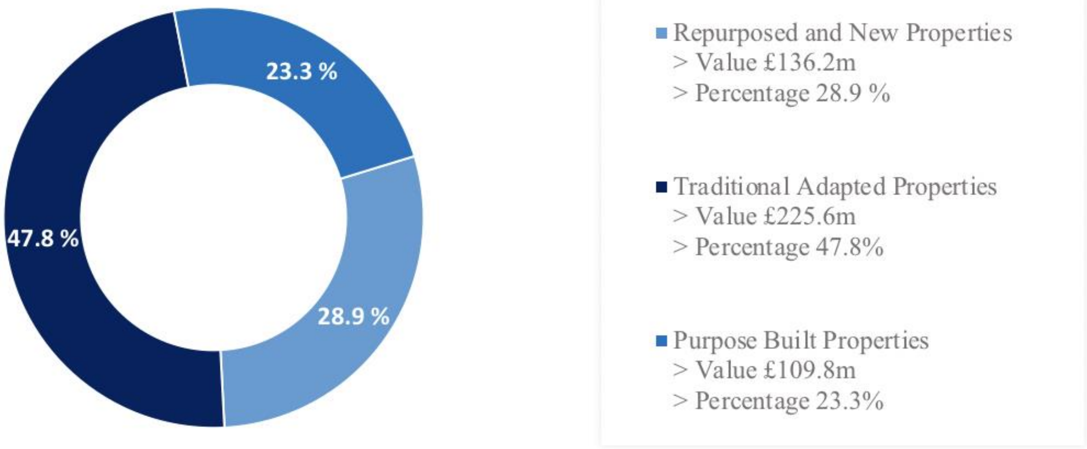
Our Properties

We have a broad mix of properties comprising traditional, specially adapted homes within the local community; purpose-built properties catering typically for a higher acuity need within the community; and newly built or reconfigured properties that have been built or adapted to cater for specific requirements for an area. In the latter case these properties can offer a very positive outcome having often previously been underutilised office or general care buildings. These buildings can be fully renovated and repurposed to become part of the specialist supported housing sector for the long-term benefit of incoming tenants and the regeneration of the local community.

It is important to act as a catalyst to bring properties into the social housing sector for the first time (new and repurposed properties). At the time of writing, these types of properties account for 28.9% of our portfolio and represent an important addition to the stock of social homes within the specialist supported housing sector. This activity forms part of our social impact assessment, enabling us to help local authorities and housing associations to meet their significant underlying needs.

Today the portfolio is divided as follows:

Portfolio by Property Type



Note: Data as at 20 March 2018

To date we have purchased 414 properties, across 109 local authority areas, contracted to 11 housing associations, working in partnership with 64 care providers and providing homes to 2,618 underlying tenants.

We seek to acquire our properties from a variety of off-market sources, including from housing associations, care providers, developers, and corporate or private owners. At the same time we are ourselves increasingly responsible for the generation of a considerable number of transactions where we bring together all the parties and introduce the homes to the social housing sector for the first time.

We have included some photographs and a short description below to illustrate several of the new and purpose-built properties that we have acquired, each of which is subject to a full repairing and insuring lease with a housing association. At the time of our next NAV and results announcements we intend to profile the broad range of our properties more fully as the portfolio continues to grow and diversify.

Care Provision: Mental Health and Learning Disabilities
South East London
22 Tenancies

Care Provision: Mental health and Learning Disabilities
Midlands
12 Tenancies

Care Provision: Mental Health
South London
28 Tenancies

Due Diligence

Regardless of the source of properties, we ensure that a detailed programme of due diligence is undertaken. First and foremost, this commences with understanding the commissioning and demand needs of each local authority, together with the needs of specific individuals. We consider the underlying long-term supply of and demand for specialist supported housing and then benchmark the rents. We do this through our own consultants (former local authority officers) as well as by comparison to our own rents database, which is now one of the largest in the sector.

Where we consider rents are too high, we seek to reduce them to a median level for the property specification. To the extent that vendors are not prepared to make such rent reductions, we will reject these properties.

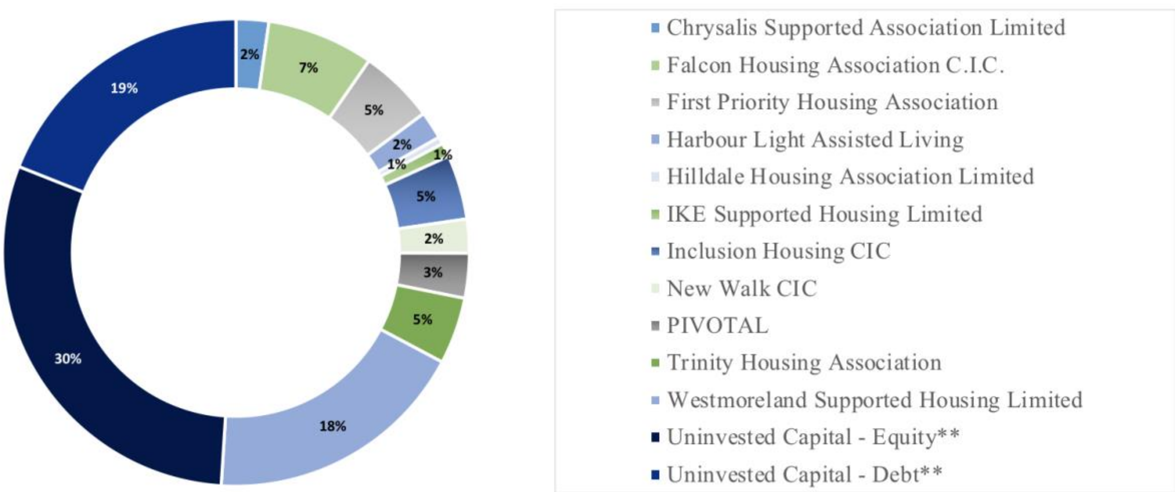
To date, we have rejected around £150m of property during the due diligence process for a variety of reasons. These include rent levels, property condition, counterparty, size of rooms and property configuration. Also, a far greater value of properties have not entered our formal due diligence process, where it is clear they did not meet our investment objectives.

With each of our property transactions we have continued to assess and evolve our due diligence and investment processes, as well as the structures that are put in place to ensure the long-term integrity of our investments. The events around First Priority Housing Association have allowed us to drive this process further, with the ambition of enhancing not just our own investments but also the specialist supporting housing sector generally. We plan to say more about this and our investment protocols at the time of our next NAV results.

Housing Associations

We work with a range of housing associations with which we seek to build long-term relationships. Today we have 11 housing association partners with which we are building strong relationships and this number will grow over time. Going forward, we intend to allocate properties to new housing associations and also those associations with which we have fewer properties today. The table below sets out existing housing associations and weightings across our Gross Asset Value for both CSH and CSHC combined.

Percentage of Gross Asset Value* by Housing Association



** Gross Asset Value is the aggregate value of the total assets of the Group once fully invested based upon the Net Asset Values as at 31st December 2017, announced on 9th February 2018 and 30% gross leverage*

*** Uninvested capital represents undeployed existing equity and debt (based on 30% gross leverage) targeted to be invested in 2018*

Note: The aggregate maximum exposure to any single housing association is 25 per cent of the Gross Asset Value, once the capital of the Group is fully invested (Source: Prospectus 18 October 2017)

By way of background, there are today c.1,500 housing associations in England and Wales of which approximately 100 manage or own over 1,000 properties each, with the balance of c.1,400 housing associations owning fewer than 1,000 properties each.

Specialist supported housing today is typically provided and managed by housing associations that have been established over the past decade and are now growing in size, working closely with local authorities to meet urgent needs. Often the individuals involved have personal experience of family members with learning disability and mental health issues that in many cases has driven their involvement in the sector. Several of these housing associations have broken through the 1,000-property level in recent years and so have entered the top 100. Clearly, more will do so in coming years as they continue to grow and develop into mature, professional organisations.

We work closely with all our housing association partners to encourage best practice and an institutional-standard approach. As part of regular initiatives, this week we hosted our housing associations at a private seminar at our offices, with the former head of the Homes and Communities Agency (forerunner to the Regulator of Social Housing), to participate in a forum to discuss best practice and our protocols for investment. This was a hugely productive exercise, which we intend to replicate in the future to place Civitas at the centre of best practice in the sector.

Income Flow

On a number of occasions, we have been asked to clarify how the income flows move within the specialist supported housing sector. We refer to the chart below that we have referenced previously, which summarises the income flows. In short:

- The local authority makes a payment to the housing association in respect of rent and property services (as housing benefit), which in turn will be reimbursed by central government.
- The housing association pays the rent received as a lease payment to Civitas, retaining any balance of rent above the value of the lease payment and also retaining 100% of the property service fee.

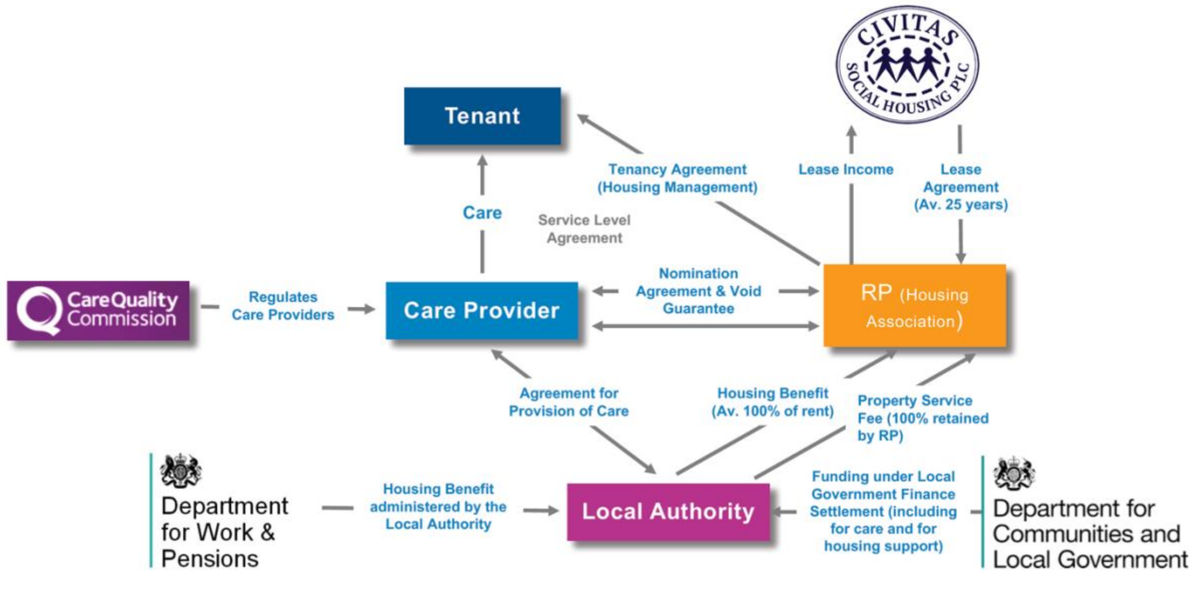


Chart to display income flows within Specialist Supported Housing

Local Authorities

We have been asked to provide more background on the manner in which the relationships between local authorities and care providers/housing associations are structured, particularly around security of income. The starting point to consider is that the local authority acts as the commissioning authority with the ambition and legal responsibility (The Care Act 2014 and other legislation such as the Homelessness Reduction Act 2017) to provide long-term, safe and stable accommodation for vulnerable adults for whom it has responsibility to provide accommodation. In turn the local authority awards care contracts to regulated care providers and works with regulated housing associations, which provide or manage accommodation.

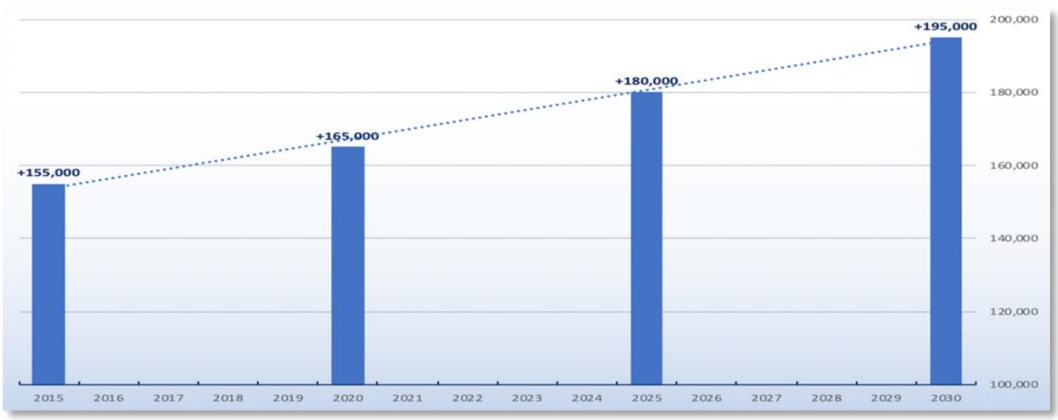
In some instances, a formal nomination agreement is entered into by the local authority, but, in the majority of cases, it is a rolling commitment on the part of the local authority to meet care, rent and property service costs. This is a system that is long-standing, well understood and familiar to the counter-parties. There is very significant and growing demand for supported care within the community, based around specialist supported housing. The drivers for local authorities are to secure additional accommodation as an appropriate base from which to provide high-quality care and support and to meet that demand.

Scale and Demand

By way of illustration of the scale and demand, the diagrams below focus on one of five current care categories of specialist support housing in which Civitas invests. Within learning disability, it is estimated that in 2015 there were c.155,000 adults with severe or critical learning disabilities housed and/or cared for in accommodation funded by local authorities or central government – much of which was based upon larger institutions outside the local community. This number is estimated to grow to c.180,000 by 2025 and more thereafter.

Civitas Specialist Social Housing verticals by client type

Estimated number of adults with high acuity learning disabilities in UK using social care services 2015 -2030



Note: In 2016/17 1 in 218 people in England were recorded as having Learning Disability, equivalent to approximately 252,000 people (Source: NHS)

It is the local authority, with the care provider, that determines which person will occupy a particular property and the timing of that occupation, and this is largely based upon clinical decisions. To our knowledge across the 109 local authority areas in which we own properties today, this system provides the security that the local authority will meet costs in the future, which are themselves reimbursed by central government. Our tenants are typically in their 30s, and in many cases a tenant is likely to remain in residence for many years, or indeed decades. Specialist supporting housing is a cost-effective and socially positive form of provision compared to more institutionally based accommodation, which is being phased out over time. In the event that a tenant leaves a property or care provision the place is filled from extensive waiting lists (across the different levels of care acuity) as with other sectors of social housing.

Pipeline and Vendors

We continue to evolve our investment pipeline both within the various framework agreements that we have signed and with new counter-parties. Whilst we have seen new capital come into the market since our launch, and existing investors continuing to invest in the sector, we are pleased to have been able to maintain our approach to pricing and quality of assets. We do not intend to be the highest bidder but remain successful in securing properties within our targeted range. We put most of this down to our track record evidenced by undertaking almost 50 transactions since launch and the manner in which we conduct ourselves during the acquisition process, together with the growing reputation of the team within the sector. We look to forge long-term partnerships with a range of carefully selected vendors. In practice, a vendor for whom price is the sole determinant is unlikely to undertake a transaction with Civitas. Without doubt, we would never agree a purchase price that we are uncomfortable with simply to secure properties and we will never purchase properties just to meet investment deadlines. We take the time required to build out a high-quality, diverse and socially important portfolio of properties of which we are proud, and we remain on track with our roll-out plans to date.

Vendors

With all our transactions to date, we are clear that as a result of the requirements of our due diligence and transaction management (rent/void deposits, maintenance deposits, property improvements, reduction in rents, acquisition costs underwritten) we have reduced the margins achieved by certain vendors and enhanced the overall security of the asset class. With most of the vendors we deal with, this approach has received widespread support as they share our long-term view of the sector and wish to recycle capital into new social homes to support the sector for many years to come. It is with parties such as these that we concentrate our efforts.

We often acquire properties that, before acquisition by us, have been through significant repurposing and redevelopment, and this will increase their capital values compared to previously reported sale prices. In recent instances we have a number of examples of former large family homes or properties with an older care setting being fully refurbished and repurposed and converted into modern self-contained flats for learning disability and mental health before they are acquired by us to become part of the social housing sector. Typical near-term profit margins agreed by vendors are often now below a usual residential developer's margin.

First Priority Housing Association

We reported in February that First Priority Housing Association had itself contacted the Regulator of Social Housing as a result of encountering cash-flow issues. We are working closely with the association and with the other interested counter-parties and will make a further announcement as soon as we are in a position to do so. It is important to remember that the estate managed by First Priority has tenants and these vulnerable individuals remain in place. One of our primary concerns, and indeed that of First Priority is that the tenants do not suffer any disruption. Given our progress to date, working with First Priority and the Regulator of Social

Housing, we are advised that the tenants remain unaffected, and this will continue as we play our part in working towards an orderly outcome. Secondly, we want to reach a successful resolution and outcome for both Civitas shareholders and First Priority.

Clearly, this event has created some short-term uncertainty for the sector and investors, and markets are keen to see how the situation is resolved. We fully understand these sentiments and we would like to reassure investors that we are working hard to help achieve a resolution.

As a result of this event and as part of our regular planned activities and interaction we are working ever-closer with our housing association partners, evolving further levels of due diligence and protections for shareholders. The recent seminar we described earlier in this note is a good example of how we are working to create best practise in the sector, forming close alliances with both housing associations and the Regulator of Social Housing. We hope you will appreciate we are limited by what we can say at the present time, but we will be able to share more about the situation and lessons learned once the position is resolved.

Summary

In summary we firmly believe, and are told by senior sector professionals, that Civitas is making a significant and positive contribution to the social housing sector since we entered the market in 2016. We care passionately about the long-term positive role that Civitas and private capital can play in the sector and we will continue to ensure that we achieve both sustainable economic and social outcomes.

We would like to thank you for your support and the confidence that you have placed in Civitas as well as your patience around First Priority. We will do our very best to keep you fully informed as we move forward and complete the further investments and reach a resolution regarding First Priority.

Yours sincerely
Civitas Housing Advisors