Homes & Communities Agency

QUARTERLY SURVEY OF PRIVATE REGISTERED PROVIDERS

2013/14 Quarter 2

Introduction

The September 2013 quarterly survey report is based on responses from the 266 private registered providers (PRPs) of social housing who own or manage more than 1,000 homes.

The survey shows that the sector continues to access sufficient finance and to manage its exposure to the risks of a challenging operating environment. Overall, the survey results continue to indicate that the sector as a whole remains financially strong.

The introduction of welfare reforms has meant that providers have been implementing plans to manage the impact on their cash flows. This has included the removal of the spare room subsidy. The Regulator will continue to monitor income collection to ensure that providers manage their financial position.

Summary of findings

- The sector's total reported borrowing facility is £69.0billion.
- £57.6billion is currently drawn, leaving undrawn facilities of £11.4billion.
- Cash available to the sector was reported to be £3.5billion (June £3.5billion).
- New facilities arranged in the quarter were reported by providers to total £1.1billion (June £556million).
- Capital market funding, including private placements, contributed 38% of the new funding in the quarter.
- Over the next 12 months the sector forecasts drawdowns of £5.9billion (June £5.8billion).
- 91% of respondents continue to anticipate that current debt facilities are sufficient for more than 12 months.
- 49 PRPs continue to make use of free standing derivatives. The notional value of standalone derivatives was reported at £9.3billion (June £9.5billion).
- The current reported mark-to-market (MTM) exposure net of unsecured thresholds is £1.1billion; collateral of £1.5billion has been given, in the form of property or cash.
- On affordable home ownership (AHO), 1,969 first tranche sales were achieved in the quarter (June 1,948); 2,976 remained unsold (June 3,304), of which 1,221 had been unsold for over six months (June 1,292).
- There were 1,589 AHO completions and acquisitions in the quarter (June 1,533).
- Pipeline AHO completions expected in the next 18 months were 17,773 (June 14,406).
- Total asset sales of £643million (June £472million) were achieved in the quarter generating a profit of £206million (June £148million).
- The increase in asset sales reflects the seasonal trend experienced in previous years for a dip in June followed by increases in successive quarters.
- Whilst it is difficult to draw conclusions at this early stage, there is no indication of significant adverse performance in arrears, voids and rent collection compared with business plans for the majority of providers.

Operating context

UK economic indicators show GDP to have continued to grow in the second quarter of 2013, with an initial estimate of 0.8% growth. Inflation figures for September remained above target with CPI at 2.7%, RPI 3.2% and CPIH 2.5%.

Average weekly earnings (excluding bonuses) were reported by ONS to have risen by 0.8% in the year to August 2013. This real term reduction in incomes combined with reduced benefits will increase the need for providers to actively manage income collection.

The Bank of England base rate has remained at 0.5% since March 2009. Three month sterling LIBOR also remained low at 0.52% in September. Providers have therefore continued to benefit from low interest rates on their variable rate debt. However, providers will need to continue to monitor and review exposure to fluctuations in interest rates in setting treasury management strategies.

Housing market data showed increases in property prices over the year to September. The Nationwide house price index for Quarter 3 showed prices to have risen in all regions of the UK. The average UK house price was reported to have risen by 4.3% over the year to September 2013. This headline average covered regional variations ranging from an increase of 10.0% for London and 0.2% for the North of England.

Income collection

The Sector Risk Profile (September 2013) identified changes in welfare reform as a strategic risk to be managed by providers. The risk profile of affordable rent and market rented products was also highlighted as a risk to be managed, along with changes to rent policy from 2015. These factors will all impact on the operating environment, reinforcing the need for well managed income collection to maintain cash flows.

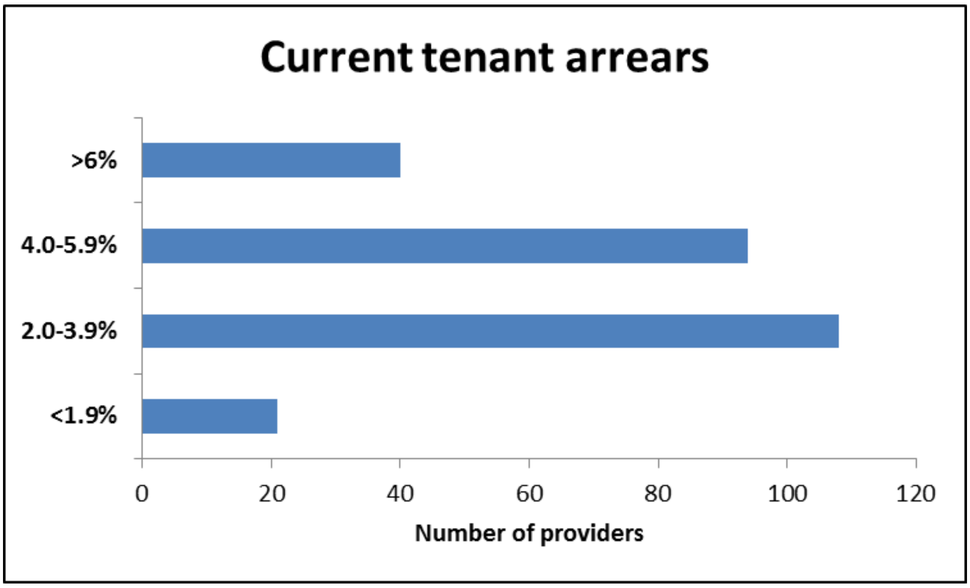
In Quarter 2, additional questions were added to the survey to begin to assess the impact of the operating environment on income collection and cash flow. The initial results from the additional questions suggest that providers are currently managing this risk and are maintaining their cash flows within business plan parameters. Rent collection figures provided at any single point in time can be influenced by the impact of payments in advance, and collection of previous arrears. It is therefore difficult to draw a significant conclusion from the initial figures. This data will form a baseline from which future trends will be monitored. The survey asked for percentages for current tenant arrears, rent collection and voids[1]. Providers were also asked to provide narrative comments on their performance in these areas.

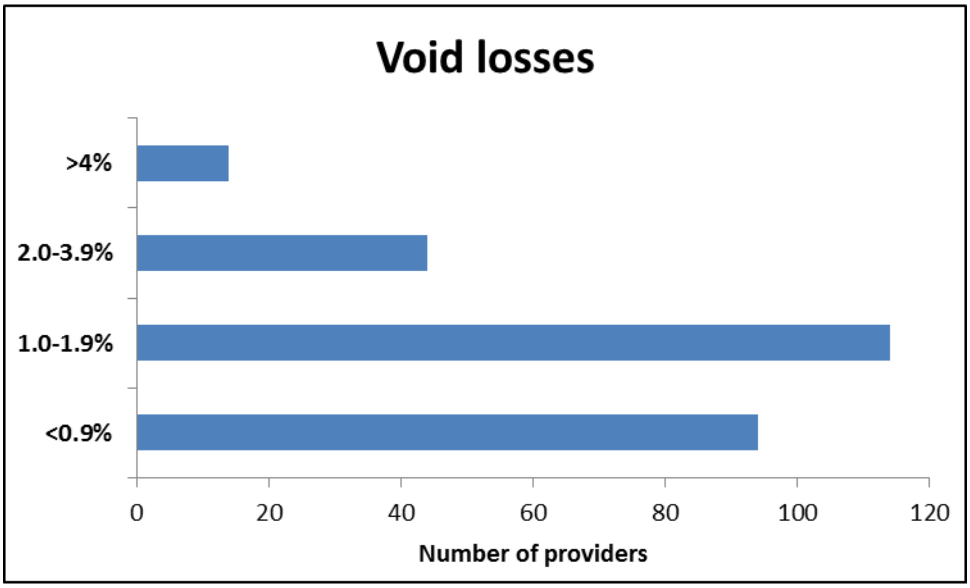
The charts below demonstrate that two thirds of the providers report current tenant arrears below 5%; the sector average based on the latest annual accounts data is 4.8%. Over three-

[1] We asked for current tenants' rent arrears as a percentage of annualised rent receivable; the percentage of rent receivable collected in the year to date and the percentage of rent receivable lost through voids in the year to date.

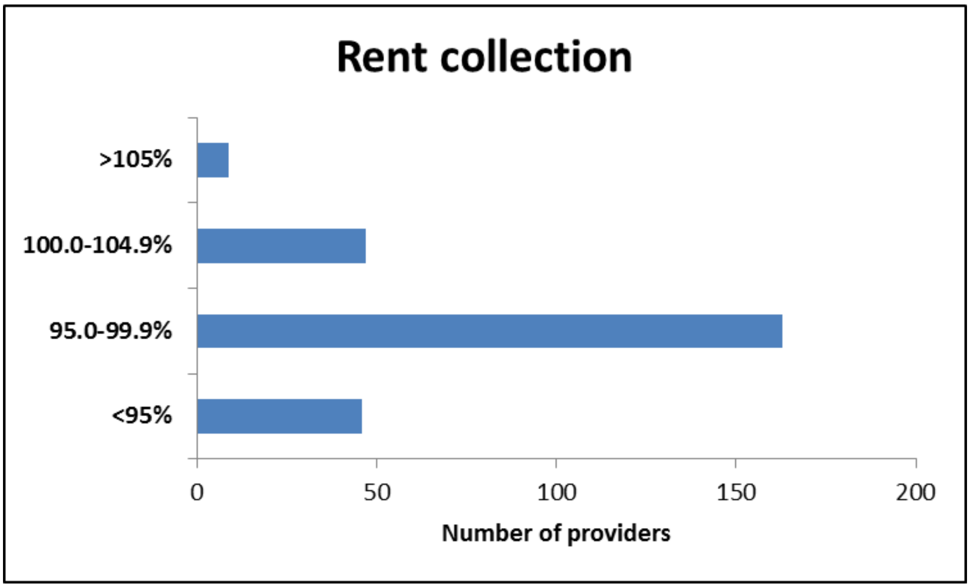
quarters report void losses of lower than 2% and the sector average is 1.75%. Rent collection figures show that over four fifths of providers report rent collection for the year to date to be in excess of 95%[2].

Most providers (88%) reported that the current levels of arrears, rent collection and voids were within or outperforming their business plans. However, these plans are typically based on assumptions that there will be a degree of adverse impact from welfare reforms. In the main, providers have allowed for a higher level of rent arrears in their plans compared to previous years. Where performance was reported to be worse than the current business plan, losses from void properties attracted the most comments. A small number of providers mentioned higher volumes of voids in larger properties and suggested that this may be attributable to under occupation. This will be monitored through future regulatory engagement with those providers.





[2] Rent collection may exceed 100% where rents have been paid in advance or previous arrears have been recovered.



Housing market

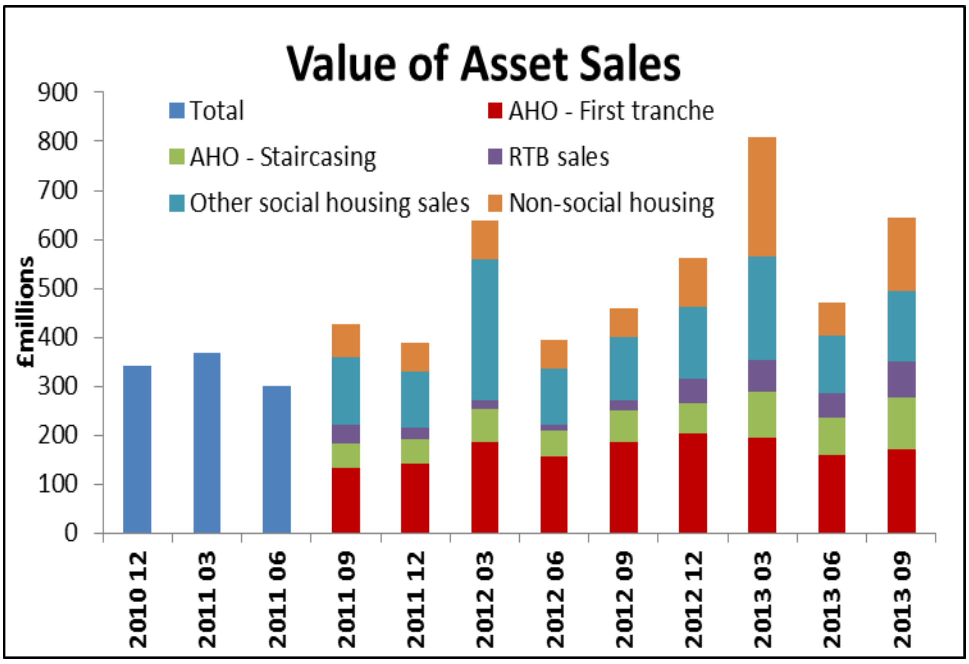
Providers develop properties for sale on the open market, which includes affordable home ownership (AHO) properties and properties for outright sale. As a result, the sector remains exposed to fluctuations and regional variations in the housing market.

The sale of AHO properties continues to be a significant activity within the sector. The sector is currently benefitting from a wider upturn in the housing market, with a reducing trend of numbers of unsold homes and of those unsold for over 6 months continuing in Quarter 2.

The Quarter 2 figures show[3]:

- 1,589 AHO homes were acquired or developed (June 1,533)
- 1,969 were sold (June 1,948)
- 2,976 remained unsold (June 3,304)
- The number unsold for over six months decreased to 1,221 (June 1,292)

[3] There is a reconciliation difference between units reported as unsold in quarter one and quarter two. This is due to a number of factors, including short term timing differences in providers recording units as completed and available for sale.



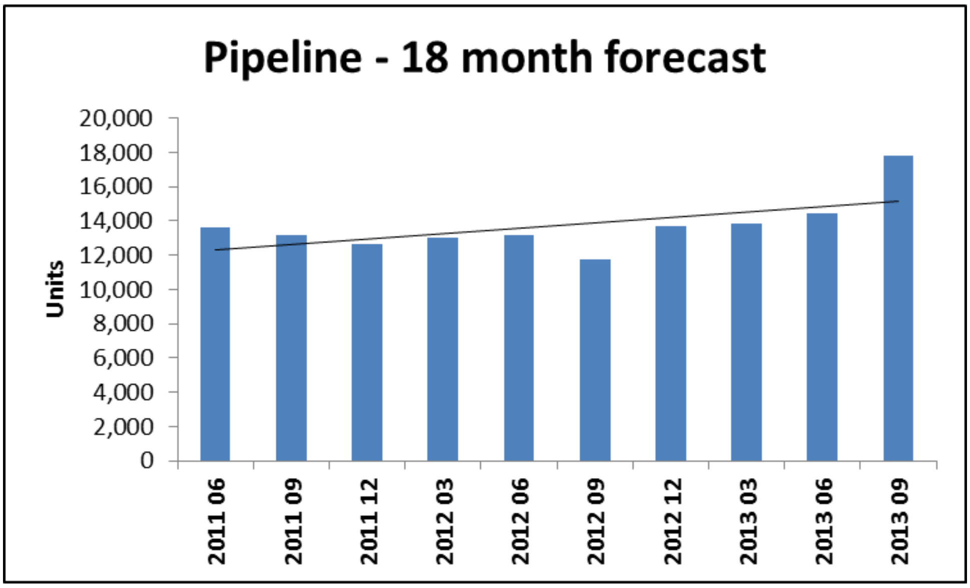
Total revenue from asset sales (including AHO first tranche and staircasing, Right to Buy (RTB), other social and non-social housing) was £643million (June £472million). Surpluses on sales were reported at £206million (June £148million).

Revenue and surpluses were higher in all categories in Quarter 2. Income from first tranche sales was £171million, with surpluses of £35million. Staircasing sales were £78million. Income from RTB sales was £71million. As stated in previous quarters, income from RTB sales does continue to provide cash to the sector. However, the longer term risks associated with the loss of rental income and the replacement of this stock do need to be managed.

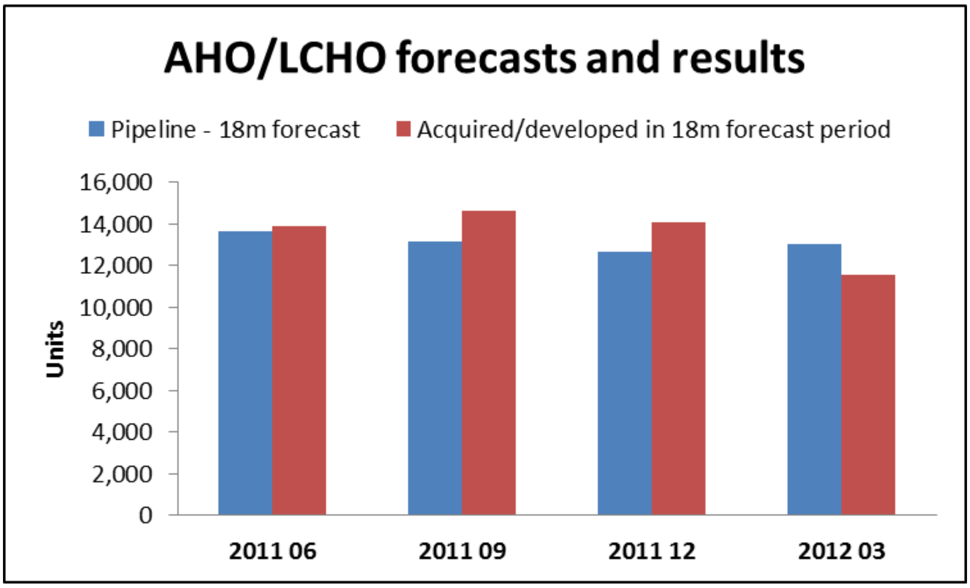
Other social housing sales of £144million included stock rationalisation sales to other providers which does not represent a loss of stock from the sector.

Development forecasts and delivery

The numbers of AHO/LCHO properties forecast to be completed within the next 18 months have shown an increasing trend over the period of the survey, with 17,773 pipeline units reported. This is an increase of 23%, 3,385 units, on the pipeline forecast in the previous quarter. Most of the increase (3,000) in pipeline units is attributable to ten providers. The pipeline forecast exceeds the units acquired and developed in the preceding 18 months by 53%. This 18 month period represents the end of the Affordable Homes Programme 2011-15 delivery period and, in line with the forecast programme profile, more activity was expected in this period. This suggests a challenging target for some and the Regulator will engage with those providers to gain assurance that the risks associated with development programmes and cashflows are controlled and monitored by boards.



The survey trend data suggests that providers' forecasts have historically been based on realistic assumptions and that affordable homes have, to date, been delivered in line with the forecasts. Pipeline 18 month forecast data has been compared to reported completions in the following six quarters for each of the quarterly surveys in 2011/12. As demonstrated in the chart below, the actual reported completions exceeded forecasts in three of the four quarters.



Financing market

New facilities arranged in the quarter totalled £1.1billion. This was a significant increase on the previous quarter, but remained below the levels reported in each quarter of 2012/13. New finance was raised in Quarter 2 from banks and from bond finance. The mix of new funding sources remained unchanged from Quarter 1, with one third being raised from capital markets and two thirds from banks. New funding raised through bank loans totalled £657million and capital market funding totalled £402million.

The sector currently reports facilities of £69.0billion, of which £57.6billion is drawn leaving undrawn facilities of £11.4billion. Cash available to the sector was reported to remain at £3.5billion.

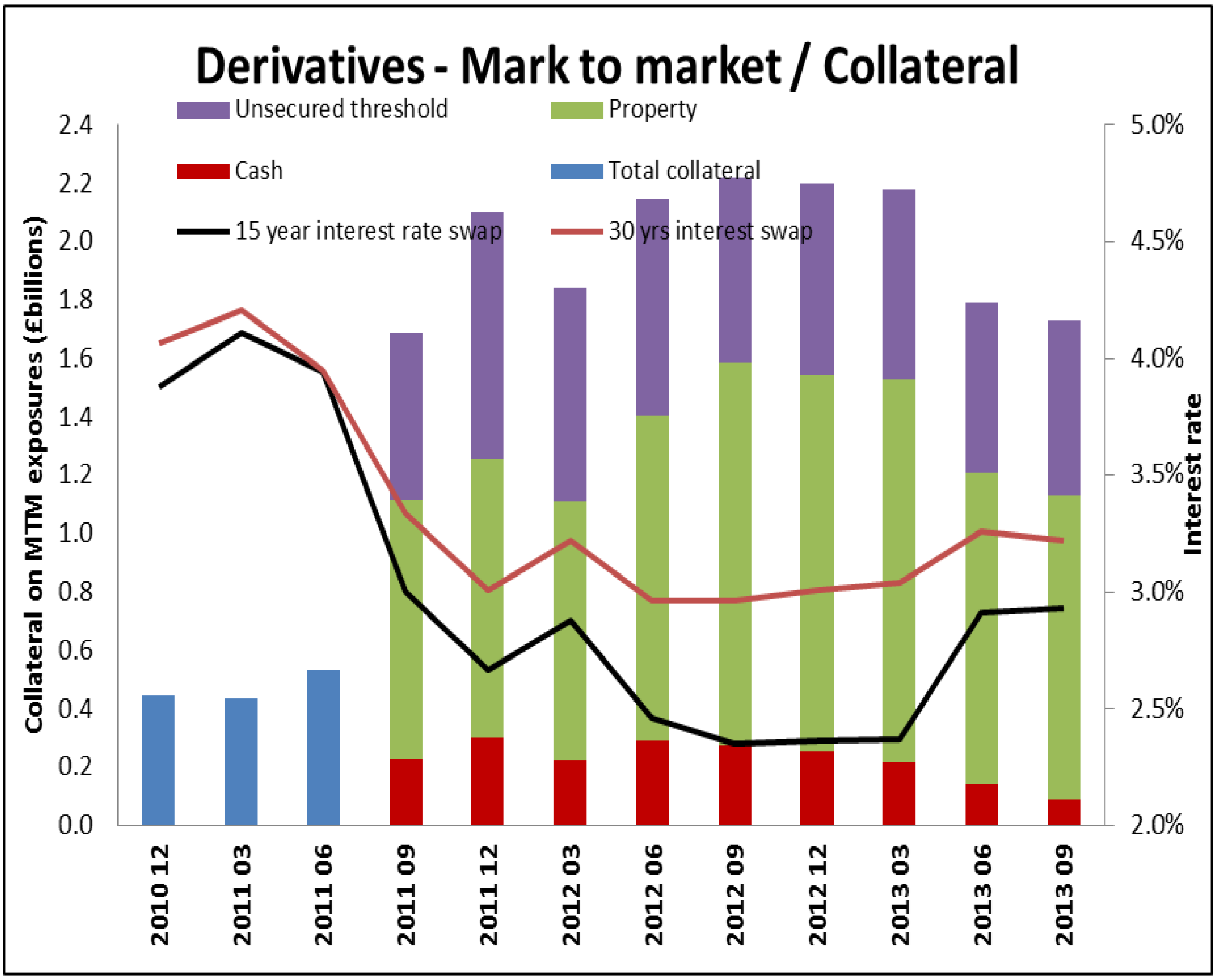
Security is reported to be in place for £65.8billion of debt, representing 95% of the agreed facilities. At sector level there is sufficient funding in place to cover the £5.9billion forecast drawdowns over the next twelve months. At provider level, the Regulator will continue to actively engage with providers reporting less than 18 months available facilities.

Derivatives

The number of providers reporting that they make use of free standing financial derivatives continues to be 49. The nominal value of the instruments is £9.3billion (June £9.5billion). The average term of these instruments remains at fifteen years. Potential interest rate volatility means that collateral requirements will remain a long term exposure. The Regulator will continue to monitor this exposure and assess its management as part of its viability reviews of individual providers.

At sector level, collateral given in terms of security and cash continues to exceed current exposure levels and to provide some mitigation against liquidity risk which remains as interest rates continue to be volatile.

Excess collateral of £411million has been given by 19 providers, providing assurance that these providers are able to withstand future interest rate changes. The mark-to-market (MTM) exposure net of unsecured thresholds is reported to be £1.1billion (June £1.2billion). Collateral of £1.5billion in the form of property and cash has been given against this exposure. Cash collateral now stands at £91million (June £137million). The Regulator will continue to monitor exposure to cash calls.



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