Regulator of
Social Housing

Quarterly survey for Q1

April to June 2019

September 2019

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Introduction

1. This quarterly survey report is based on regulatory returns from 218 private registered providers (PRPs) and PRP groups who own or manage more than 1,000 homes.

2. The survey provides a regular source of information regarding the financial health of PRPs, in particular with regard to their liquidity position. The quarterly survey returns summarised in this report cover the period from 1 April 2019 to 30 June 2019.

3. The Regulator reviews each PRP's quarterly survey. It considers a range of indicators and follows up with PRP staff in all cases where a risk to the 12-month liquidity position is identified. We have assurance that all respondents are taking appropriate action to secure sufficient funding well in advance of need.

Summary

4. The quarterly survey findings are:

- The sector remains financially strong with access to sufficient finance:

  - £20.4 billion of undrawn facilities are in place. Debt facilities total over £97 billion.

  - Cash balances total £5.3 billion; this is forecast to reduce in the next 12 months to £3.4 billion as cash is used to fund planned capital expenditure.

  - New finance of £1.4 billion was agreed in the quarter, including £1.2 billion from banks and £0.2 billion from capital markets.

  - Loan repayments of £0.7 billion were made in the quarter.

- Performance in the quarter indicates that the operating environment was challenging in some respects, reflecting wider economic uncertainties particularly around Brexit. However, this has not destabilised the sector's overall strong financial position:

  - Cash interest cover, excluding current asset sales, was 107% in the quarter to June 2019 against a forecast of 126%. The shortfall is due to an increase in working capital requirements in quarter 1. This seasonal effect has been observed in previous years. Interest cover is forecast to improve to 134% over the next 12 months.

  - Including both current and fixed asset sales, total sale receipts were £1.1 billion in the quarter, generating surpluses of £0.3 billion. However, current asset sales receipts were more than 40% below forecast at £0.7 billion.

  - Investment in housing supply was £3.1 billion in the quarter to June 2019; slightly lower than the March forecast contractually committed spend for the quarter of £3.3 billion.

- During the quarter 3,275 Affordable Home Ownership (AHO) units were developed and 3,218 units were sold. There was a 2% increase in the number of unsold units to reach 7,031 at the end of June; the highest level in ten years. Half of the unsold AHO units were held by 17 providers.
- During the quarter there was a 56% increase in the number of AHO units unsold for more than six months, which reached 2,133 at the end of June.

- During the quarter 1,193 market sale units were developed and 1,015 were sold. The number of unsold properties increased by 7% to 2,073, the highest level recorded since the data was first collected in June 2014. The number of properties unsold for more than six months reduced by 13% to 554. Over half of the total unsold market sale units are held by six providers.

- The number of AHO and market sale completions, and the increase in the number of unsold units, reflects an overall trend of increased development activity. Total completions, under these tenures, during the quarter were 17% higher than the corresponding quarter of the previous year.

- The sector's spending on capitalised major repairs in the quarter was around £400m, 20% below forecast. The main reasons for this variance relate to delays in starting new contracts for works and to the re-profiling of programmed works. Quarterly variances in cashflows are to be expected in large programmes of major repair works.

- Providers making use of free-standing derivatives reported mark-to-market (MTM) exposure of £2.3 billion, a 3% increase since March reflecting a decrease in swap rates at the quarter end. In aggregate providers continue to have headroom on available collateral on MTM exposures.

- Income collection data continues to show a stable performance consistent with seasonal trends.

- Forecasts for the next 12 months indicate that the sector is planning to increase its development and housing market exposure, supported by drawing additional debt. There is some flexibility in these plans:

  - In the 12 months to June 2020 the sector is forecasting £5.4 billion worth of current asset sales and £1.7 billion of fixed asset sales. By comparison, in the 12 months to June 2019 current asset sales were £3.2 billion and fixed asset sales were £1.8 billion. Net debt is forecast to increase by £4.7 billion.

  - Over the 12-month forecast period expected investment in new housing supply is £16.1 billion, of which £11.2 billion is contractually committed. In the 12 months to June 2019 total investment in new supply was £12.1 billion.

  - Development of for-sale properties (both AHO and market sale) is forecast to continue to increase. In the next 18 months, including committed and uncommitted development, plans include the completion of 32,936 AHO units and 13,165 market sale properties. This compares to 22,053 AHO units and 7,429 market sale properties developed in the last 18 months.

Regulatory expectations

5. PRPs are expected to manage their resources effectively to ensure that their viability is maintained, particularly during a period of significant uncertainty. The Regulator continues to follow up cases where financial indicators such as interest cover are weaker to ensure that PRPs are managing their risks effectively. The Regulator also continues to monitor developments in the housing market closely and engage with providers with significant exposures to market and AHO sales. PRP boards should be aware of the flexibility in their plans, and deploy it as necessary if the operating environment deteriorates.

6. Before contractually committing to development spending, the Regulator expects PRP boards to: carefully consider market conditions; model cashflows and viability impacts under a range of economic assumptions; and ensure that access to any external finance required is in place. This is particularly important where housing market exposure is involved. The Regulator expects providers to have contingency plans in place for market and AHO sales falling short of forecasts.

7. The Regulator also expects PRP boards to ensure that its properties are in a good state of repair and meet all applicable statutory health and safety requirements.

Operating environment

8. The housing market is currently challenging in some parts of the country, including reductions in house prices. Inflation and construction costs remain relatively stable.

9. Key metrics for the period covered include the following:

   - The average house price in England[1] increased by 0.7% in the year to June 2019. Along with the annual increase to May which also stood at 0.7%, this is the lowest annual increase to have been experienced since 2012. The greatest level of growth was in the East Midlands, where prices increased by 3.2% over the year. London experienced the lowest annual growth, with prices falling 2.7% over the year. There were also reductions in annual prices in the South East of 0.6%, and in the South West of 0.2%.

   - The Consumer Prices Index (CPI)[2] rose by 2.0% in the year to June 2019 (year to March 2019: 1.9%). Forecasters currently predict that inflation will be at 1.8% for the year ending December 2019 and 2.1% for the year ending December 2020[3].

   - Construction Output Price Index (OPI) figures[4] for all construction showed that costs increased by 3.0% in the year to June 2019.

10. The survey results demonstrate that the sector is in a strong position in terms of liquidity, and has sufficient cash and undrawn facilities to respond to further changes and challenges within the wider economic environment.

11. Some of the results for this quarter in respect of sales of newly developed housing stock are indicative of challenging conditions in which to operate the cross-subsidy model of development. This is where profits generated from developing homes for sale are used to subsidise development of social tenures. While forecasts show that the sector intends to pursue the cross-subsidy model at an increased scale in the next 12 to 18 months, there is flexibility within forecast spending commitments.

12. The key risks faced by the sector are considered in the Sector Risk Profile[5] published annually by the Regulator. The Regulator will continue to monitor key market trends and to seek assurance that boards of PRPs are actively engaged in responding to emerging risks.

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[1] Office for National Statistics: UK House Price Index England
[2] Office for National Statistics: Consumer price inflation, UK: June 2019
[3] HM Treasury: Forecasts for the UK economy: a comparison of independent forecasts. August 2019
[4] Office for National Statistics: Construction Output Price Indices (OPIs), UK: April to June 2019
[5] https://www.gov.uk/government/collections/sector-risk-profiles

Private finance

13. The sector's total agreed borrowing facilities are £97.7 billion, £60.0 billion (61%) of which are bank loans.

14. £77.3 billion is currently drawn, leaving undrawn facilities of £20.4 billion. After a peak in undrawn facilities of £20.8 billion last quarter, this is the second highest amount of available facilities ever reported by the sector.

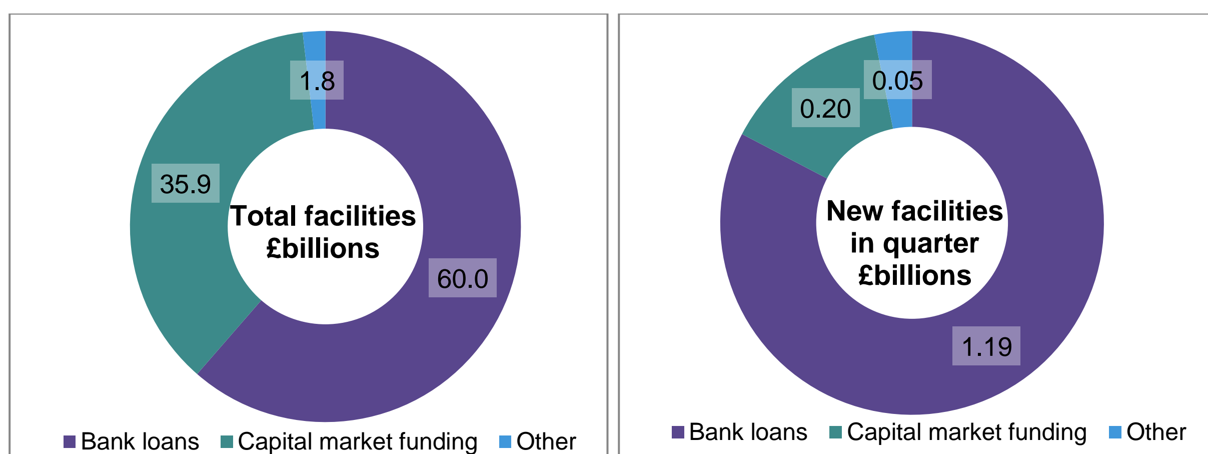
15. 97% (March: 97%) of providers forecast that current debt facilities are sufficient for more than 12 months.

16. At a sector level, current cash and undrawn facilities (£25.8 billion) are more than sufficient to cover forecast net expenditures for the next year (£9.1 billion), even if no new debt facilities are arranged.

17. In the 12 months to June 2020 the sector is forecasting loan drawdowns of £7.0 billion (March 12 month forecast: £6.6 billion), of which £1.4 billion is from facilities not yet agreed (March: £0.8 billion).

18. During the quarter 20 providers arranged new funding. New facilities agreed, including refinancing, totalled £1.4 billion. This is the lowest amount of new finance arranged in a single quarter in the last two years; however undrawn facilities remain high following a record level (£4.5 billion) of new finance having been arranged in quarter four of 2018/19. £0.7 billion worth of loans were repaid during the quarter.

19. Bank lending accounted for 83% (£1.2 billion) of new funding in the quarter. Capital market funding, including private placements and aggregated bond finance, contributed 14% (£0.2 billion) and other sources, including local authority lending, contributed 3%.



20. Of the £97.7 billion agreed facilities, £89.2 billion has been secured and £4.5 billion of facilities do not require security. There are further agreed facilities of £4.0 billion where security is not yet in place.

Cashflows

21. It is essential that providers have access to sufficient liquidity at all times. The Regulator engages with PRPs that have low liquidity indicators or are forecasting drawdowns from facilities not yet agreed or secured.

Summary cashflow forecast[6]

Figures in £ billions	3 months to 30 June 2019 (forecast)	3 months to 30 June 2019 (actual)	12 months to 30 June 2020 (forecast)
Operating cashflows excluding sales	1.0	0.9	4.5
Interest cashflows	(0.8)	(0.8)	(3.3)
Payments to acquire and develop housing	(4.0)	(3.1)	(16.1)
Current assets sales receipts	1.1	0.7	5.4
Disposals of housing fixed assets	0.4	0.4	1.7
Other cashflows	(0.2)	(0.3)	(0.5)
Cashflows before resources and funding	**(2.5)**	**(2.2)**	**(8.3)**
Financed by:			
Net grants received	0.4	0.3	1.5
Net increase in debt	0.7	1.0	4.7
Use of cash reserves	1.4	1.0	2.1
Total funding cashflows[7]	**2.5**	**2.2**	**8.3**

22. Interest cover, based on operating cashflows excluding sales, was 107% in the quarter to June 2019 (March 2019: 157%). This compares to a forecast of 126% made in March 2019. The reduction in interest cover compared to forecast is due to lower than anticipated operating cashflows excluding sales, which were £0.1 billion less than the £1.0 billion forecast. Increased cash outflows have been attributed to movements in debtor and creditor balances, including the payment of large annual costs in advance. Operating cashflows are expected to strengthen over the next 12 months, increasing the projected interest cover over the forecast period to an average of 134%.

23. In the 12 months to June 2020 the sector is forecasting £5.4 billion worth of current asset sales, of which £4.9 billion relates to properties for which development is contractually committed. Current asset sales receipts in the quarter were £0.7 billion, around one-third down on forecast. In the 12 months to June 2019 current asset sales of £3.2 billion were achieved.

24. In the 12 months to June 2020 the sector is forecasting £1.7 billion worth of fixed asset sales. In the 12 months to June 2019 fixed asset sales were £1.8 billion.

[6] Operating cashflow excludes current asset sales receipts and costs of sales. ‘Payments to acquire and develop housing properties’ include payments in respect of both current and fixed assets.

[7] There are rounding differences in the calculated totals; figures are reported by providers in £000.

25. Expenditure on new supply in the quarter totalled £3.1 billion. This was below the forecast of £4.0 billion, and slightly less than the £3.3 billion forecast expenditure on contractually committed schemes. To some extent this demonstrates flexibility for a large proportion of capital spending.

26. Capitalised repair and maintenance expenditure in the quarter amounted to £430 million, 21% less than the £547 million forecast. Variances have been attributed to delays in commencing programmes in the new financial year and re-profiling of planned works.

27. In the 12 months to June 2019, capitalised expenditure on repairs and maintenance was £1.9 billion. In the 12 months to June 2020 the sector is forecasting capitalised repairs and maintenance expenditure of £2.3 billion.

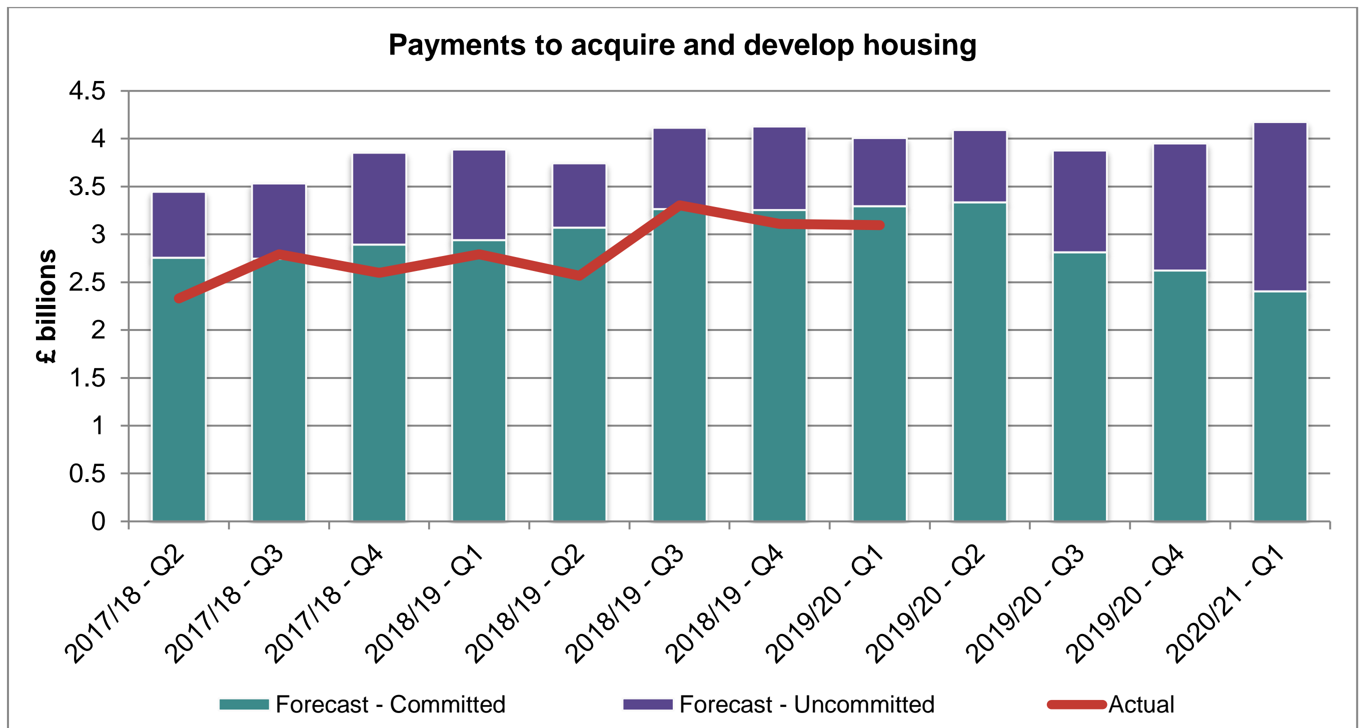
28. Cash balances reduced by £1.0 billion during the quarter as reserves were used to fund capital expenditure. This was below the forecast reduction in cash from March of £1.4 billion.

29. Cash available at June 2019 was £5.3 billion, the lowest available balance in nearly four years. This is forecast to reduce further to £3.4 billion over the next 12 months as cash reserves are used to fund capital investment.

30. In addition to the £5.3 billion available, cash held in secured accounts (and therefore not accessible to providers) totalled £0.8 billion at June 2019 (March 2019: £1.0 billion).

Development

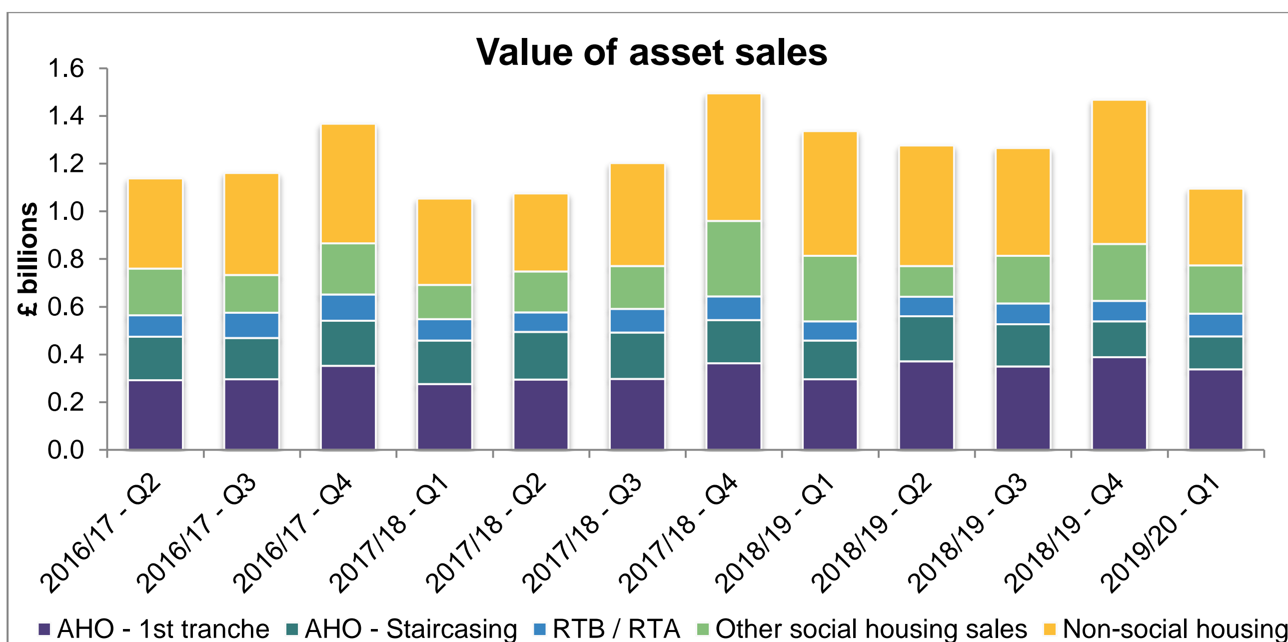
31. In the 12 months to June 2019, £12.1 billion was invested in the acquisition and development of housing properties. In the next 12 months £11.2 billion expenditure is committed to acquire and develop housing properties, and a further £4.9 billion of uncommitted expenditure has been forecast.



32. Actual expenditure in the quarter ending June 2019 was £3.1 billion, equal to the amount reported in the previous quarter. This was below the total forecast expenditure of £4.0 billion, and the £3.3 billion forecast on contractually committed schemes. Development programmes are subject to change and the variances are largely a result of timing differences and slippage. Providers consistently exercise prudence in their forecasts by over estimating expenditure on development.

Housing market

33. Total asset sales amounted to £1.1 billion in the quarter to June 2019, a decrease of 18% compared to the corresponding quarter of 2018/19, but equal to the sales achieved in the same quarter of 2017/18. Surpluses from asset sales were £0.3 billion, giving a margin on sales of 31%.



34. Fixed asset sales for the quarter amounted to £0.4 billion; 11% higher than the amount forecast in March 2019. Current asset sales in the quarter (market sales and first tranche AHO sales) were £0.7 billion; 41% less than the forecast of £1.1 billion.

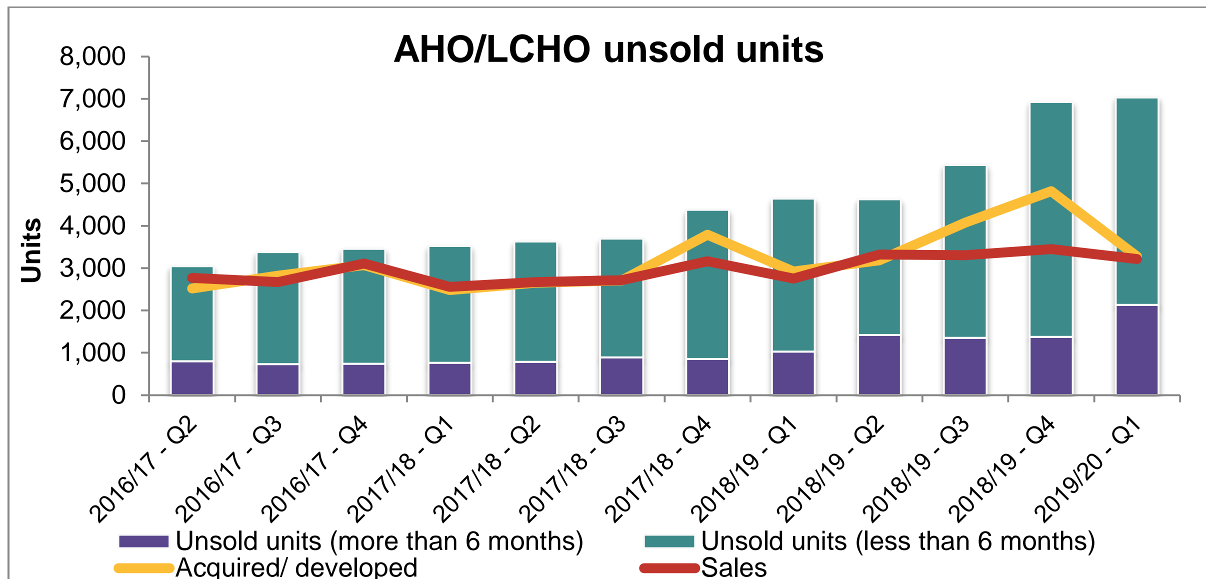
35. AHO sales were 3,218 units (March: 3,448) compared to the 3,275 completions reported in the quarter (March: 4,817). The total number of unsold AHO units increased by 2% to reach 7,031 at the end of June (March: 6,924), the highest level in ten years. The number of units unsold for more than six months increased by 56% to 2,133 (March: 1,371). The total number of unsold units was impacted by net transfers of 78 units that were converted to AHO from other tenures.

36. Half of the unsold AHO stock at the end of the quarter was held by 17 providers. These 17 providers all have access to sufficient finance, with each holding between £0.2 billion and £0.9 billion worth of cash and undrawn facilities. Between them this amounts to £7.8 billion, or 30% of the total facilities available within the sector.

37. Of the 2,133 AHO units unsold for over six months, 49% were held by providers operating mainly in London and the South East[8], and 57% of the increase in unsold units over the quarter was experienced by providers operating in this area.

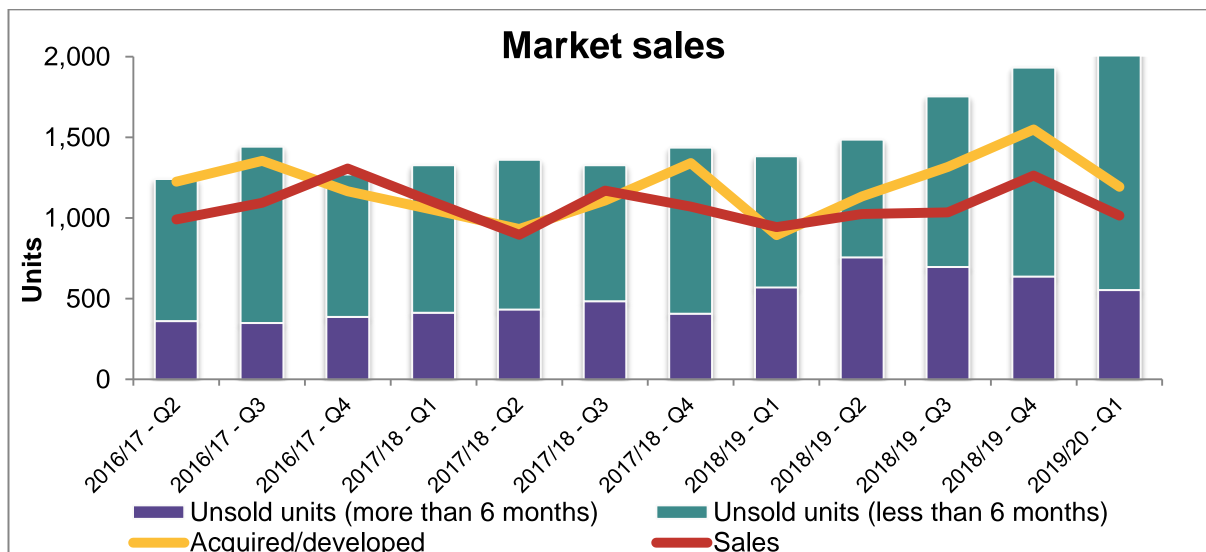
[8] Defined as providers holding 50% or more of their existing stock within the region

38. There were four providers that hold over 100 units of stock that had been unsold for more than six months, accounting for 36% of the total figure. The providers are well funded at present and have sufficient operating cashflows to maintain liquidity if sales receipts are not realised. We continue to monitor this risk on an ongoing basis and to test business plans to ensure that they are robust enough to cope with a range of adverse scenarios.



39. Development for outright market sale is concentrated in relatively few providers. There were 1,015 sales in the quarter (March: 1,263) compared to the 1,193 units developed for market sale (March: 1,550). The total number of unsold market sale units increased by 7% to reach 2,073 at the end of June (March: 1,933), the highest level recorded since the data was first collected in June 2014. The number of units unsold for over six months reduced by 13% to 554 (March: 637).

40. Over half of the unsold market sale units were held by just six providers. Between them, these six providers have access to £3.4 billion worth of cash and undrawn facilities.



41. The number of both AHO and market sale completions in the quarter, and the number of unsold units at the end of the quarter, reflect an overall strategy of increasing development activity. In total, completions of AHO and market sale units were 17% higher than in the corresponding quarter of the previous year.

42. The pipeline of AHO completions expected in the next 18 months is 32,936 (March: 31,901) of which 26,362 are contractually committed. This is an increase of 49% compared to the 18 months to June 2019, when there were 22,053 AHO completions. For market sale, 13,165 (March: 13,783) completions are expected in the next 18 months, of which 11,994 are contractually committed. This is 77% higher than the 7,429 market sale completions achieved in the 18 months to June 2019.

Derivatives

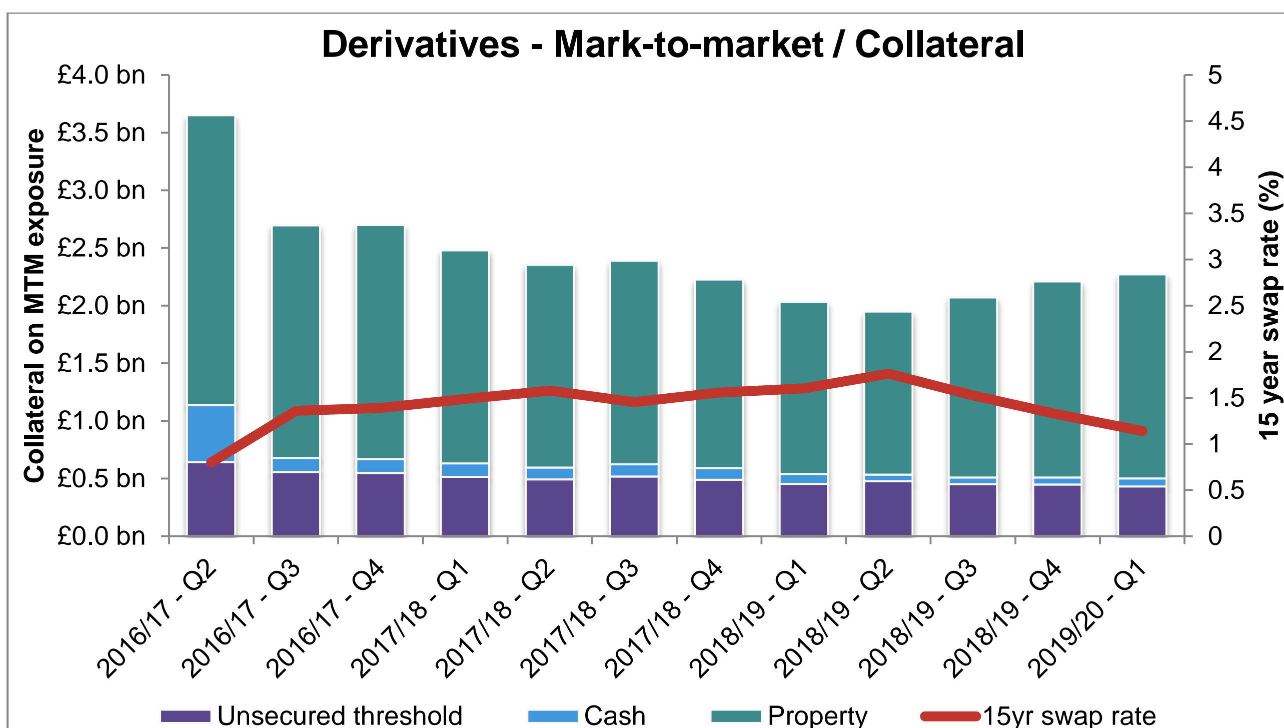
43. Forty providers (March: 41) currently make use of free-standing derivatives.

44. At the end of June the notional value of standalone derivatives was £8.6 billion (March: £8.3 billion).

45. The current gross MTM exposure increased by 3% from March to £2.3 billion.

46. Unsecured thresholds and available security pledged to swap counterparties was £3.4 billion. Of this total collateral, £1.9 billion (March: £1.9 billion) had been employed in the form of property or cash, together with unsecured thresholds of £0.4 billion.

47. The additional excess collateral available consists primarily of property pledged but not employed.



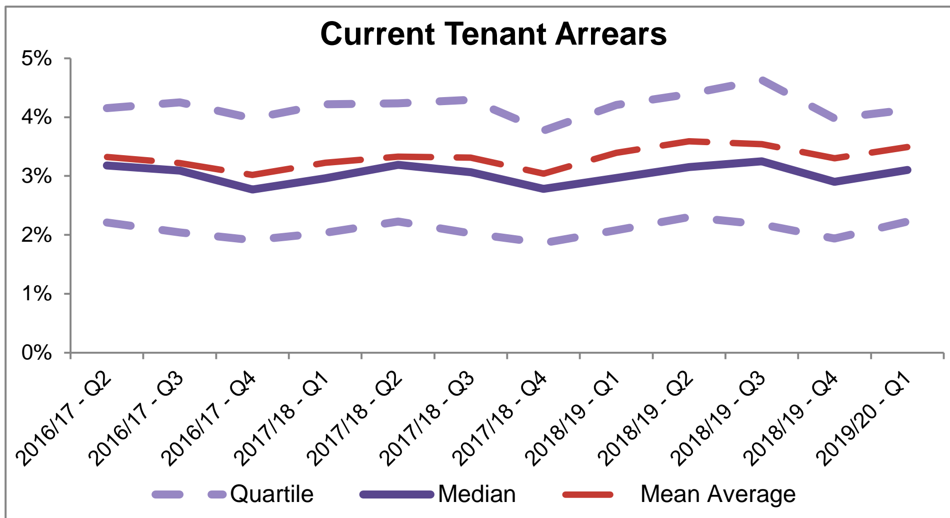
48. The above graph shows MTM exposures excluding excess collateral. Sterling swap rates reduced further during the quarter, resulting in an increase in MTM exposure.

49. Collateral given in terms of security and cash continues to exceed the sector's current exposure levels; this provides some mitigation against the risk of further adverse movements in the swap rate. At sector level, the headroom of collateral available over current exposure was £1.2 billion, or 51%.

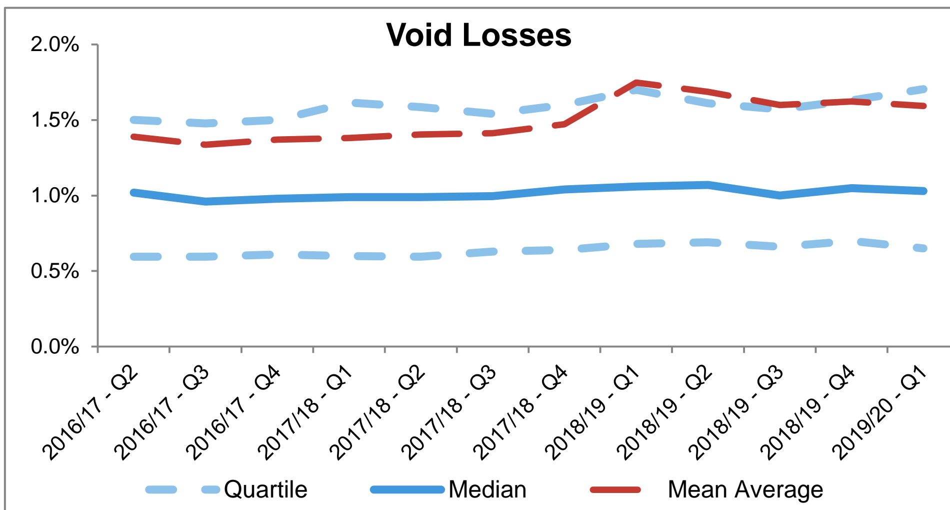
50. Interest rate volatility means that collateral requirements will remain a long-term exposure. Individual providers must ensure that they have sufficient available security as a fall in swap rates has the potential to increase MTM exposure. The Regulator will continue to monitor ongoing movements in the swap rate and to engage with providers where there are significant levels of exposure.

Income collection

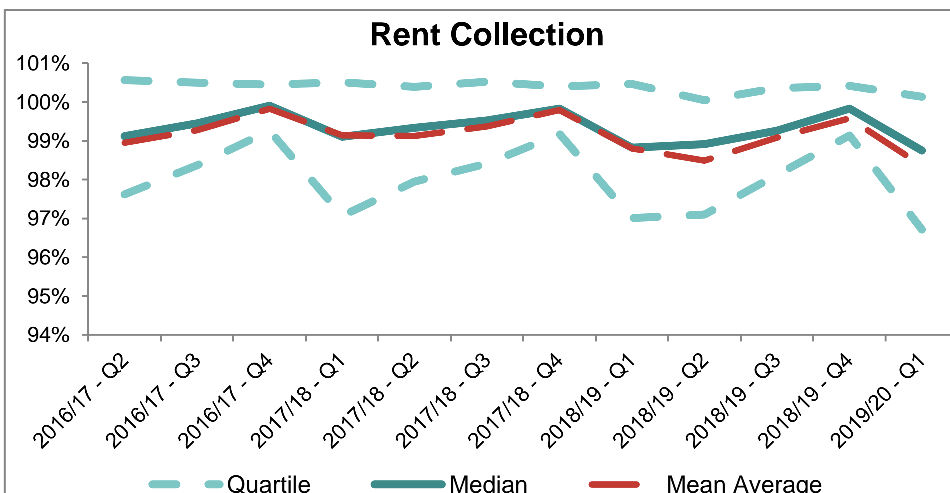
51. Most providers (86%) continue to report that the current levels of arrears, rent collection and voids are within, or outperforming, their business plan assumptions. The responses for each quarter remain reasonably stable, suggesting that providers are managing income collection risks and maintaining cashflows within business plan parameters. Fluctuations in income collection and arrears are broadly consistent with seasonal trends. Housing benefit cycles remain likely to have an impact on rent collection data.



Median and mean current tenant arrears both increased during the quarter, to 3.1% and 3.5% respectively (March: 2.9% and 3.3%). These are both slightly higher than the results for June 2018, when median arrears were 3.0% and mean arrears 3.4%. An increase in arrears between quarter four and quarter one is consistent with seasonal trends.



Median void losses reduced slightly during the quarter to 1.0% (March: 1.1%), while mean void losses remained at 1.6%. The mean average is affected by 13 providers reporting void losses of 5% or more.



Mean average rent collection rates were 98.4% during the quarter, while the median was 98.7%. These rates are slightly lower than the results from the corresponding quarter of 2018/19, when both the mean and median rent collection rates were 98.8%. 29 providers reported rent collection rates of less than 95% (March 2019: 5 and June 2018: 29).

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The Regulator of Social Housing regulates registered providers of social housing to promote a viable, efficient and well-governed social housing sector able to deliver homes that meet a range of needs.