



Homes &  
Communities  
Agency

# QUARTERLY SURVEY OF PRIVATE REGISTERED PROVIDERS

December 2014

## **Quarterly Survey of Private Registered Providers**

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### **Introduction**

The December 2014 quarterly survey report is based on responses from 255 private registered providers (PRPs) of social housing who own or manage more than 1,000 homes.

The survey results continue to indicate that the sector as a whole remains financially strong with access to sufficient finance. New finance continues to be raised through both capital markets and bank loans; the sector appears to remain attractive to lenders. Significant amounts of cash remain available to the sector; this is required to cover operating and development costs. However, individual providers and their boards do need to balance the risks of ensuring the availability of funds against the risk and costs of holding surplus cash.

Providers who make use of free standing financial derivatives have reported increased cash calls in the quarter and the head room on collateral provided to meet mark- to- market exposures has decreased in the quarter. These providers need to continue to monitor their position with regard to potential further calls.

Managing the risks of Affordable Home Ownership (AHO) development programmes, including delivery of the AHO element of the Affordable Homes Programme (AHP) 2011-15, remains a challenge. AHO development forecasts continue to anticipate a step increase in activity in the final quarter of 2014/15. Boards need to be aware of the March 2015 AHP completion deadline and the risks and costs associated with potential delays to the programme. The stock of unsold AHO units increased in quarter 3; historic trends show that a further increase in unsold AHO stock at the end of quarter 4 is likely. Providers must factor the uncertain timing of future sales receipts into cashflow planning.

Market sales activity remains concentrated in relatively few providers. The regulator engages with these providers to monitor the associated risks. As with AHO, the number of unsold units increased in quarter 3. Development is forecast to increase over the next 18 months; providers will need to continue to be aware of the risks associated with development costs and sales cash flows.

Income collection data suggests that a large majority of providers are continuing to manage the impact of welfare reform on their cash flows. To date, most large providers (92%) continue to report that the current levels of arrears, rent collection and voids are within, or outperforming, their business plans. However, this is not to underestimate the impacts which are being managed by providers. Business plans typically incorporate assumptions allowing a degree of adverse impact from welfare reform measures, and increased revenue costs are likely to be incurred to adapt to changes. The regulator will continue to monitor income collection as universal credit is rolled out.

### **Summary of findings**

#### **Private finance**

- the sector's total borrowing facilities total £74.5bn, 75% of which is bank loans
- £62.2bn is currently drawn, leaving undrawn facilities of £12.3bn

- cash available to the sector is £4.6bn (September £4.2bn)
- new facilities arranged in the quarter totalled £1.7bn
- capital market funding, including private placements, contributed 73% of the new funding in the quarter
- over the next 12 months the sector forecasts drawdowns of £5.0bn (September £4.7bn)
- 93% (September 92%) of providers continue to anticipate that current debt facilities are sufficient for more than 12 months. Providers must continue to ensure that they have secured facilities in place to cover their forecast drawdown requirements
- the number of providers continuing to make use of free standing derivatives remained at 47. The notional value of standalone derivatives was £9.3bn (September, £9.4bn)
- the current mark-to-market (MTM) exposure net of unsecured thresholds increased to £1.9bn (September £1.1bn); collateral of £2.4bn (September £2.1bn) has been given in the form of property or cash

### **Housing market**

- on AHO, 2,227 first tranche sales were achieved in the quarter (September 2,207<sup>1</sup>), 3,161 homes remained unsold (September 2,800) of which 955 had been unsold for over 6 months (September 968)
- there were 2,562 AHO completions and acquisitions in the quarter (September 1,983)
- pipeline AHO completions expected in the next 18 months are 18,515 (September 18,521)
- on market sales, 481 sales were achieved (September 774); 448 homes remained unsold (September 427), of which 169 had been unsold for over 6 months (September 112)
- there were 477 homes developed for market sale in the quarter (September 549)
- pipeline market sales completions expected in the next 18 months are 5,092 (September 5,529)
- total asset sales of £787m (September £792m) were achieved in the quarter generating a surplus of £254m (September £237m)

### **Operating context**

Headline figures indicate a continued recovery in the UK economy. The preliminary estimates released by the Office for National Statistics (ONS) showed that GDP had increased by 0.5% in Q4 2014 and was 2.7% higher compared with the same quarter a year ago.

Inflation figures for the year to December were: Consumer Price Index (CPI) 0.5%; CPI including home ownership costs (CPIH) was 0.6% and Retail Price Index (RPI) 1.6%. CPI remains below the government's target of 2%; the December 2014 rate is the joint lowest on record (CPI May 2000 was 0.5%).

As discussed in the [Sector Risk Profile \(September 2014\)](#), future rental income increases on social rented properties will be linked to CPI. Providers must continue to be mindful of the business planning implications of differential inflation rates.

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<sup>1</sup> AHO September sales amended from previously reported 2,205; 2 additional units were reported in November.

The Sector Risk Profile highlights the potential impact of welfare reform, in particular direct payment under Universal Credit (UC), on rent collection and the cash flow and covenant risks. The speed of UC roll-out is projected to increase markedly during 2015. Department of Work and Pensions expects UC to be available in 1 in 3 jobcentres by April 2015 and in all jobcentres by spring 2016<sup>2</sup>. The most substantial early impacts are likely to be felt by providers operating in the North West of England, where jobcentres are making UC available to a wider range of claimant households than elsewhere during 2015.

UK labour market statistics showed that, for September to November 2014, the unemployment rate decreased to 5.8%. 512,000 more people are in work compared with one year ago. Average weekly earnings (excluding bonuses) were 1.8% higher than a year ago.

The Bank of England base rate has remained at 0.5% since March 2009. Three month sterling LIBOR also remained low at 0.56% in December. Providers therefore continue to benefit from low interest rates on their variable rate debt. However, they will need to continue to monitor and review exposure to future interest rate fluctuations in setting treasury management strategies. The 15 year sterling swap rate fell to 2.06% in December 2014 (3.19% December 2013); further falls in the swap rate were reported in January 2015.

The Nationwide House Price Index reported increased house prices of 0.2% in December, the report showed an 8.3% increase between Q4 2013 and Q4 2014. The regional variations ranged from 1.5% in Yorkshire and Humberside to 17.8% in London.

### **Financing market**

The sector currently reports facilities of £74.5bn, of which £62.2bn is drawn leaving undrawn facilities of £12.3bn. Cash available to the sector is £4.6bn (September £4.2bn).

Cash available to the sector has been reported to be over £4bn in each of the last 4 quarters; 13 providers currently report available cash in excess of £75m; this represents 33% of the sector total. Providers do need to ensure that cash is available to cover all future financial obligations as they fall due. However, boards must balance the risks of ensuring that funds are available against the risk and costs of holding surplus cash.

New facilities arranged in the quarter totalled £1.7bn. New finance was raised from bank loans and capital market funding. 73% of the new funding came from the capital markets through bond issues, private placements and European Investment Bank funding through Affordable Housing Finance plc (AHF); 27% came from traditional bank and building society lending. The availability of new facilities continues to suggest that the sector retains the confidence of investors.

Providers are forecasting drawdowns of £5.0bn over the next 12 months. Security is currently reported to be in place for £72.0bn of debt; this represents 97% of agreed facilities and 116% of drawn facilities. At sector level, there appears to be sufficient security in place to cover the forecast drawdowns over the next 12 months. However, it remains essential for individual providers to ensure that their facilities are secured in good time to enable drawdown.

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<sup>2</sup> Universal Credit at Work - Spring 2015 (DWP, February 2015).

The majority, 87% of providers, continue to report that they have sufficient facilities in place to cover the next 18 months. However, providers need to continue to be aware of the current timescales for arranging and securing new finance. The regulator will continue to engage with providers reporting 18 months or less in respect of their available funding.

As reported in previous quarters, the maturity profile of existing debt suggests that the immediate refinancing risk of the sector remains low. Most of the new debt requirement over the next two years will be to fund providers' development programmes.

The regulator expects boards to understand the risks associated with arranging new finance and with maintaining an appropriate level of liquidity. Independent, professional advice should be taken as appropriate and boards should have the skills necessary to understand and critically appraise that advice.

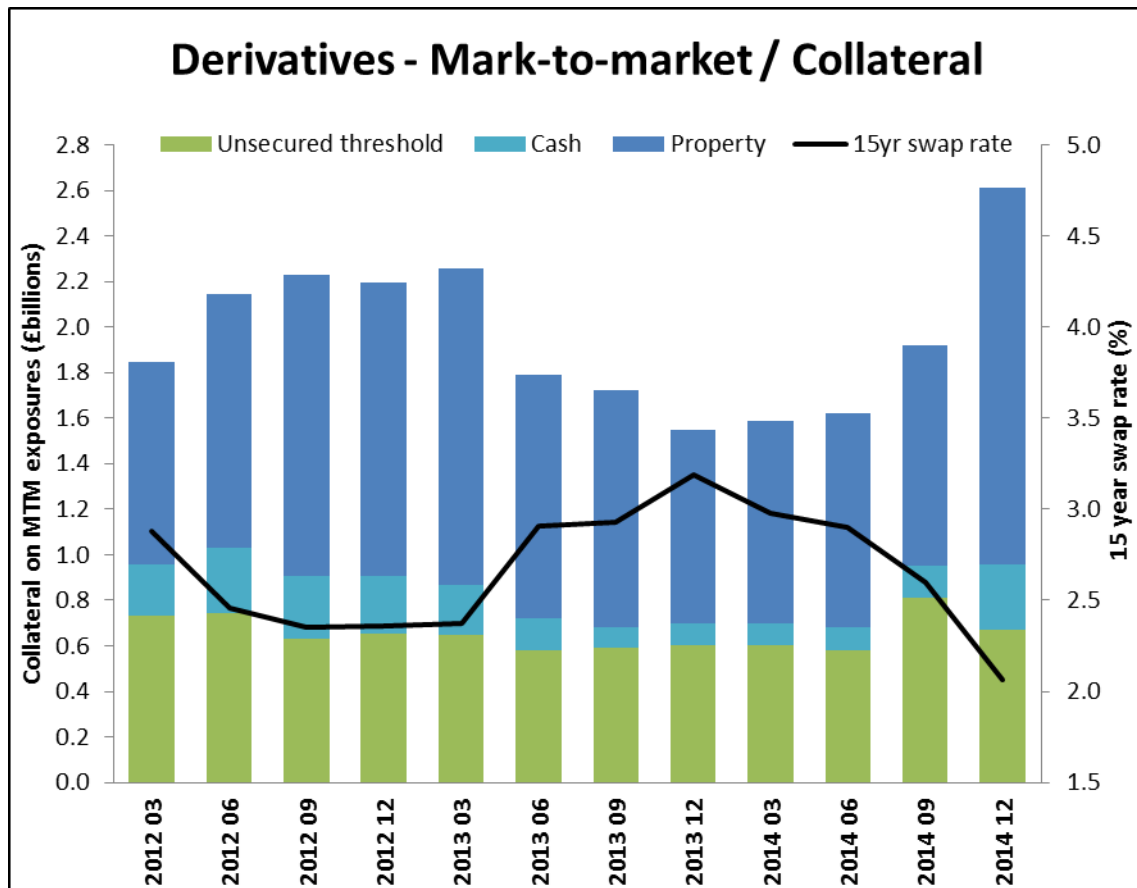
## **Derivatives**

The number of providers reporting that they make use of free standing derivatives to mitigate against interest rate fluctuations remained at 47. The notional value of the instruments is now £9.3bn (September £9.4bn). The average term of the instruments is 14.6 years.

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. In the December quarter, falling swap rates led to an increased exposure to margin calls, a trend which continued through January. The mark-to-market (MTM) exposure net of unsecured thresholds increased to £1.9bn (September £1.1bn). Collateral of £2.4bn in the form of property and cash has been given against this exposure (September £2.1bn). Posted cash collateral more than doubled to £300m (September £143m), which probably reflects a desire to maintain control over security (as withdrawing cash if rates move back up) and the speed of the increase in mark-to-market exposure; the regulator is continuing to monitor providers' exposure to cash calls.

Excess collateral, totalling £520m (September £992m) is reported by 33 providers. This does provide some assurance that these providers are able to withstand a degree of future interest fluctuations. However, this quarter's increase in exposure has significantly eroded the excess collateral and providers must continue to monitor their position with regard to potential calls for increased collateral. The aggregated position is also likely to mask under- and over-collateralisation between different counterparties within the same provider. The regulator is actively engaging with affected providers to gain assurance that they are effectively managing potential exposures to further increased margin calls.

Potential interest rate volatility means that collateral requirements remain a long term exposure. The likely impact of the adoption of Financial Reporting Standard 102 on loan covenant compliance also needs to be considered. Providers should assess their individual positions and have appropriate discussions with lenders. The regulator will continue to monitor this exposure and to assess its management as part of its financial regulation of individual providers.

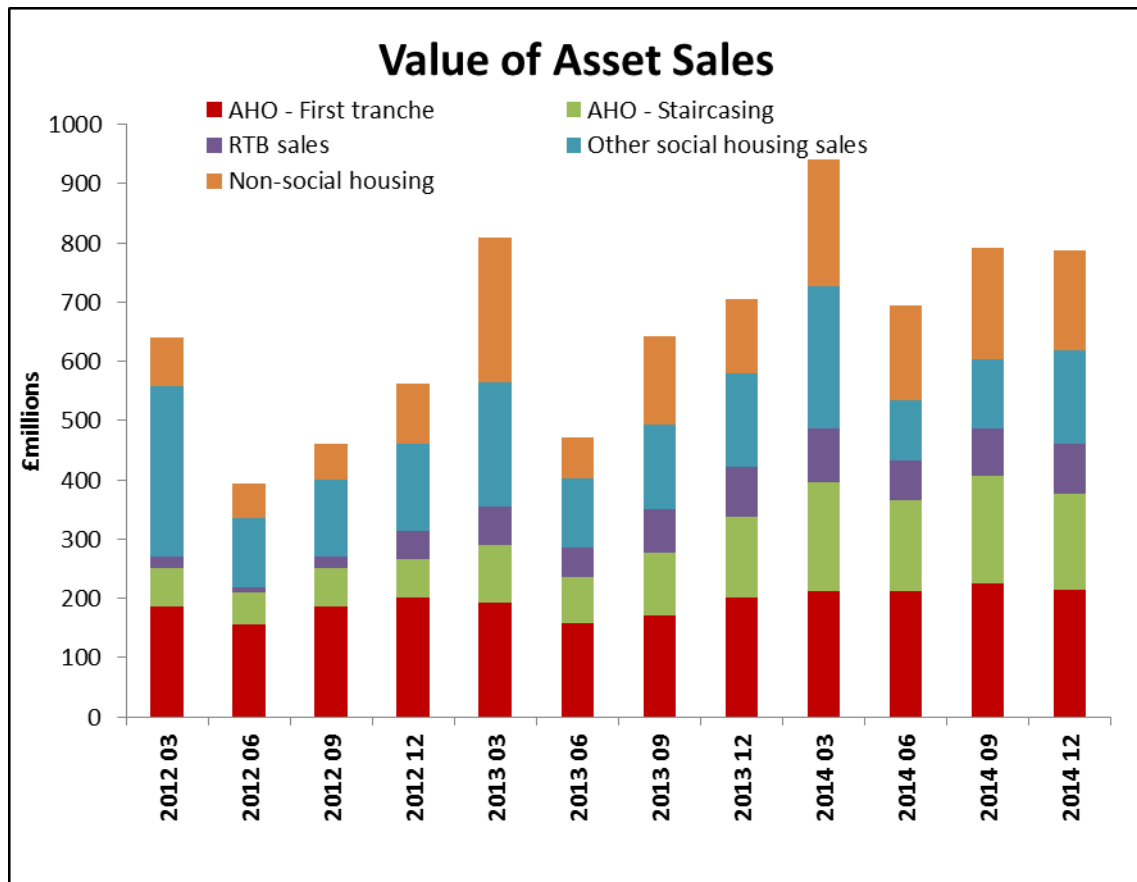


The chart above shows mark-to market exposures, excluding excess collateral, and illustrates movements in exposure relative to the 15 year swap rate.

### Housing market

The sector continues to deliver a significant sales programme. This includes shared ownership, social housing sales and market sales. Many providers aim to achieve growth through housing development including an element of housing built for sale; providers therefore need to be aware of, and manage, the impact of sales risk on their development cash flows.

Total revenue from asset sales in quarter 3 (including AHO first tranche and staircasing, Right to Buy (RTB) and other social and non-social housing) was £787m (September £792m). Surpluses on sales were £254m (September £237m). Sales revenue fell by 1% compared to September, surpluses showed growth of 7%. Both sales and surpluses were above the levels reported for December 2013. An analysis of the value of asset sales from March 2012 is shown in the chart below.



The sales figures show:

- Income from first tranche sales was £213m; the surplus was £58m. The margin of 27% was higher than both the previous quarter and a year ago (September, 24%; December 2013, 18%)
- Staircasing sales were £163m; the surplus was £64m. The margin of 39% was also higher than both the previous quarter and a year ago (September, 36%; December 2013, 29%)
- RTB sales generated income of £84m with surpluses of £33m. These sales continue to generate income for the sector, but the risks associated with the loss of future rental income and the need for replacement stock need to be managed
- Other social housing sales were £159m with surpluses of £61m. The margin of 38% was lower than in the previous quarter and a year ago (September 40%; December 2013, 54%). These sales include asset management sales, including some stock rationalisation transfers within the sector
- Non-social housing sales were £168m with surpluses of £39m. The margin of 23% was higher than the previous quarter, but lower than a year ago (September 20%; December 2013, 27%)

#### Affordable home ownership

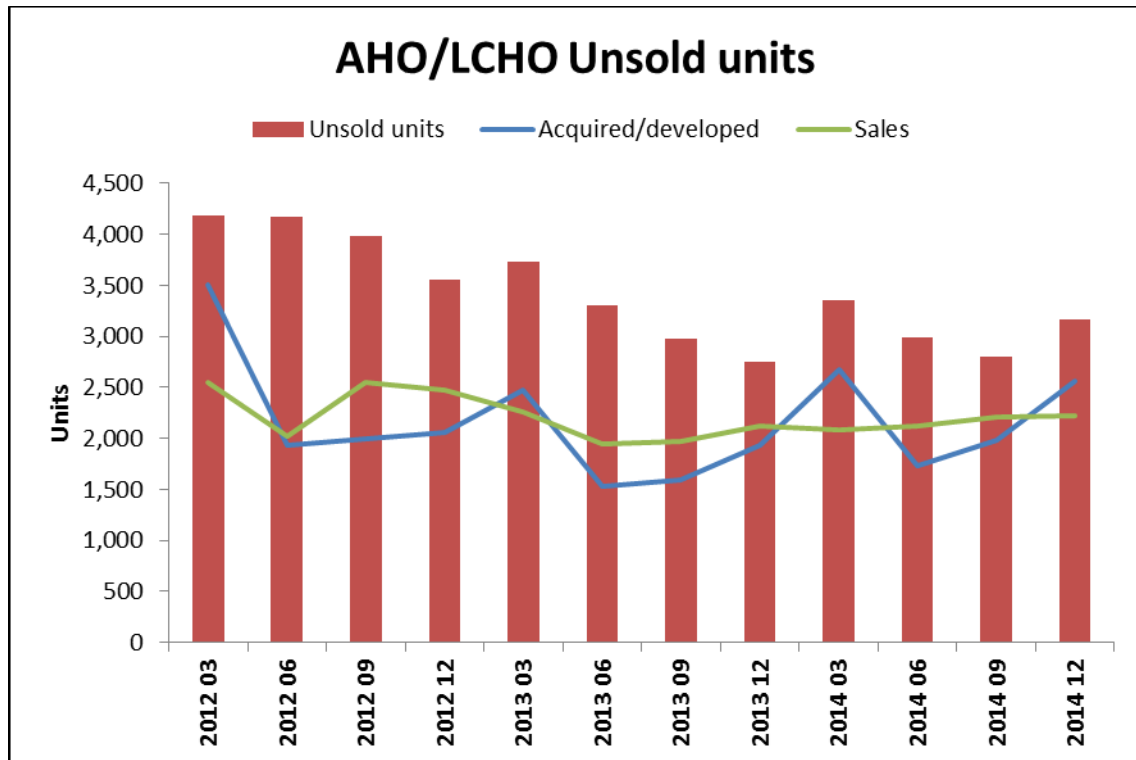
The quarter 3 figures show<sup>3</sup>:

- 2,562 AHO homes were acquired or developed (September 1,983)
- 2,227 were sold (September 2,207)

<sup>3</sup> There is a small reconciliation difference between units reported as unsold at quarter ends.

- 3,161 were unsold at the quarter end (September 2,800)
- 955 properties remained unsold for over six months (September 968)

The figures demonstrate that sales continue to take place at a good margin, reflecting the current market conditions. However, as shown in the chart below, the increase in acquisition and development in the quarter, combined with flat sales has led to an increase in the number of unsold units.



As the chart above shows, the number of units completed is a significant driver of the fluctuations in unsold stock numbers. If the forecast increase in numbers of completions is delivered in the next quarter, there will be a further increase in the numbers of properties available for sale (see below, AHO development forecasts and delivery). Providers must factor the uncertainty of future sales receipts in planning forward cash and funding requirements.

Significant levels of AHO development and sales activity are concentrated in relatively few providers; over half of all the unsold AHO stock at the end of quarter 3 is held by 20 providers. The regulator expects all providers engaging in AHO development to continue to manage the risks of housing market exposure.

### **AHO development forecasts and delivery**

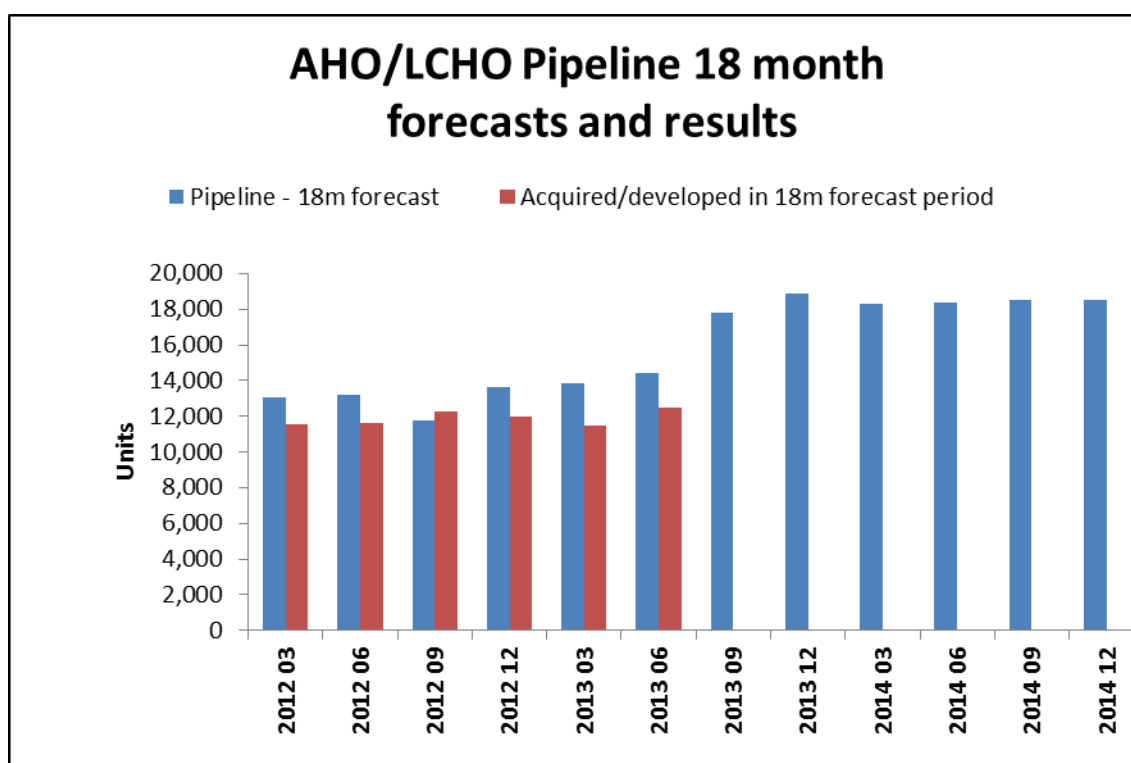
Providers report that 18,515 AHO units are forecast to be completed over the next 18 months (September 18,521). This represents 3,086 units per quarter; this is 48% higher than the average quarterly completion rate of 2,080 units over the previous 18 month period.

The September 2013 18 month pipeline forecast was 17,773 units; in the 5 quarters to date, 10,893 units have been delivered. To meet the forecast will require 6,880 completions in the final quarter; this exceeds the 6,279 completions reported in the first three quarters of 2014-15.



The 2011-15 delivery period concludes at the end of March 2015. Providers need to be aware of this completion deadline and of the risks and costs associated with any potential delays to the programme.

The track record on shared ownership completions shows that the 18 month pipeline forecast has only been achieved once in the 6 quarters from 2011-12 Q4 to 2013-14 Q1. Comparing shared ownership completions in the last 18 months against the pipeline forecast reported in June 2013 shows that actual completions for this period were 1,924 units below forecast.



The regulator continues to engage with providers to gain assurance that the risks associated with development programmes are controlled and monitored by boards. In particular, providers need to be aware of local housing market conditions and to have mitigation plans in place to deal with the potential sales risks associated with large numbers of properties becoming available for sale. Providers need to be aware of the impact on business plans from delays in completions or sales.

### Market sales

The quarter 3 figures show<sup>4</sup>:

- 477 homes were developed (September 549)
- 481 homes were sold (September 774)
- 448 remained unsold (September 427)
- 169 remained unsold for over six months (September 112)

<sup>4</sup> There is a reconciliation difference between units reported as unsold between quarter ends, this largely results from transfers between tenures.

Sales numbers continued to exceed development. However, this was by a smaller margin than in the last quarter, a small number of units were also transferred from other tenures into market sales leading to an increase in the total number of unsold units. The number of unsold units over 6 months has also increased.

Development forecasts show 5,092 homes for market sale to be in the pipeline for delivery over the next 18 months, an average of 849 per quarter. This quarterly run rate is 76% higher than the quarterly average completions over quarters 1, 2 and 3. As with AHO products, providers will need to be aware of local housing market conditions and to have regard to the risks associated with meeting ambitious sales targets. The sales risk exposure for market sales development remains concentrated in a small number of providers. The regulator continues to engage with these providers to monitor boards' understanding and management of the associated risks.

### **Income collection**

As reported in the [Sector Risk Profile \(September 2014\)](#), welfare reform remains a strategic risk to be managed by providers. The risk profile of Affordable Rent and market rented products, along with changes to rent policy from 2015, were also highlighted as a risk to be managed. These exposures reinforce the need for well managed income collection to maintain cash flows. The quarterly survey income collection questions are intended to assess the impact of the operating environment on income collection and cash flow. Data is collected for percentages for current tenant arrears, rent collection and voids<sup>5</sup>. The responses for each quarter appear to be reasonably stable and to suggest that providers are continuing to manage the risks and to maintain cash flows within business plan parameters.

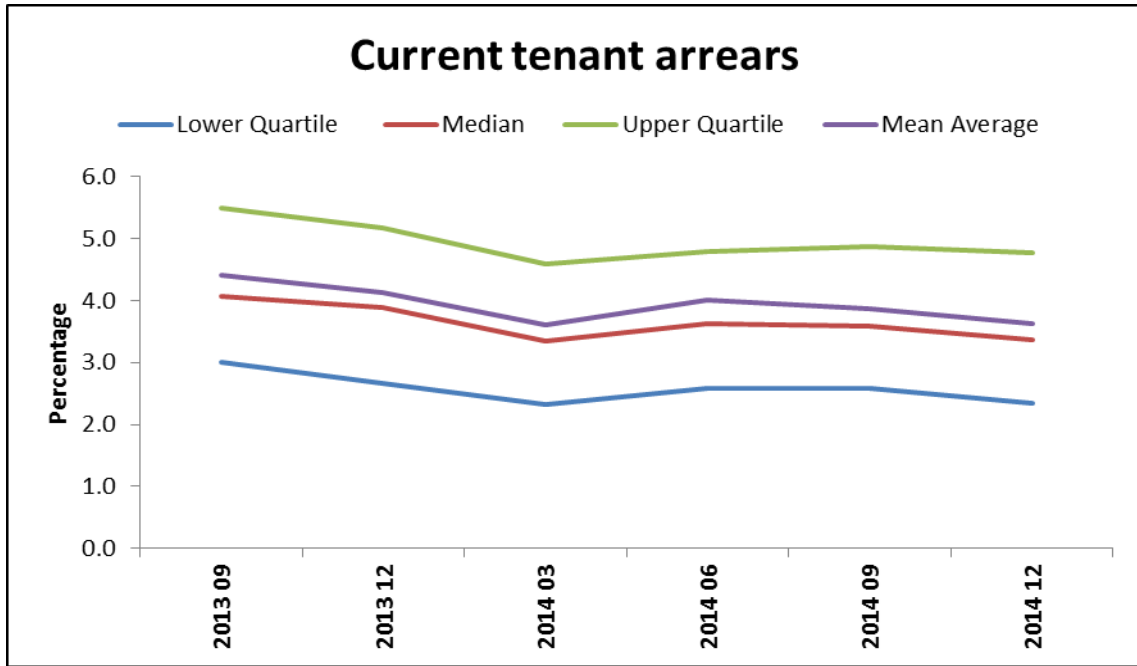
Most providers (December 92%, September 94%) continue to report that the current levels of arrears, rent collection and voids are within, or outperforming, their business plans. However, as noted in previous quarters, these plans are typically based on assumptions that there would be a degree of adverse impact from welfare reform measures.

Current tenant arrears percentages are illustrated in the chart below<sup>6</sup>.

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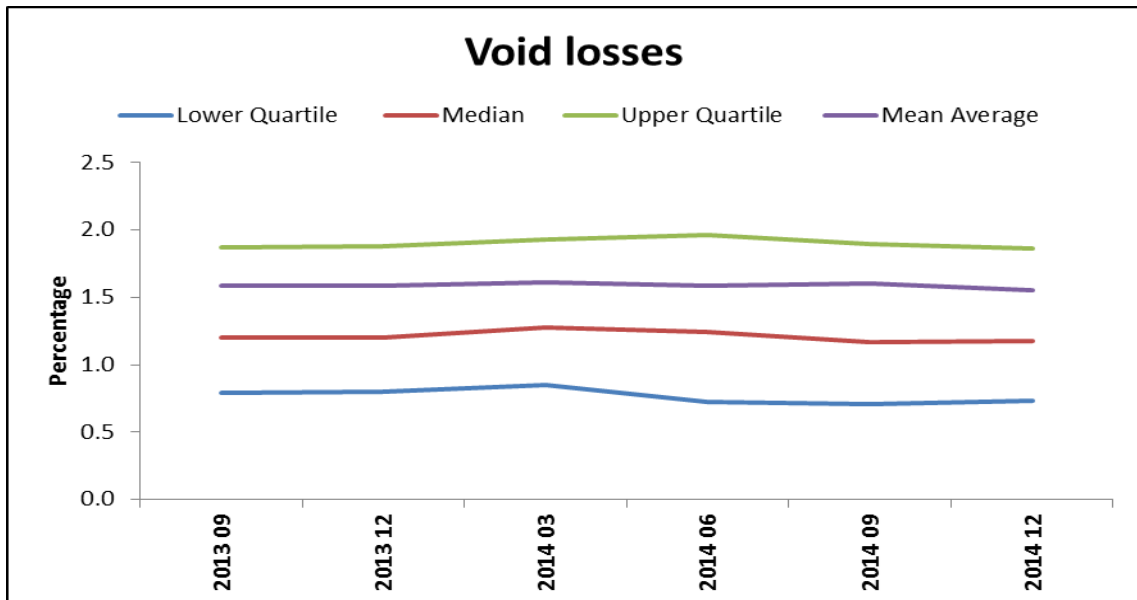
<sup>5</sup> The survey asked for current tenants' rent arrears as a percentage of annualised rent receivable; the percentage of rent receivable collected in the year to date and the percentage of rent receivable lost through voids in the year to date.

<sup>6</sup> Current tenant arrears data has been amended for September 2014: current tenant arrears mean average at September 2014 have been revised to 3.9%; previously reported at 4.2%. Providers with rent arrears below 6% has been revised to 89%; previously reported at 88%.



Of the survey respondents, 93% (September 89%), continue to report that current tenant rent arrears are below 6%. The sector aggregate current tenant arrears level, based on the latest published annual accounts data<sup>7</sup>, is 4.8%. The current tenant arrears reported this quarter showed a small decrease in comparison to the previous quarter. The mean average figure was 3.6% (September 3.9%). The median level of rent arrears was 3.4% (September 3.6%).

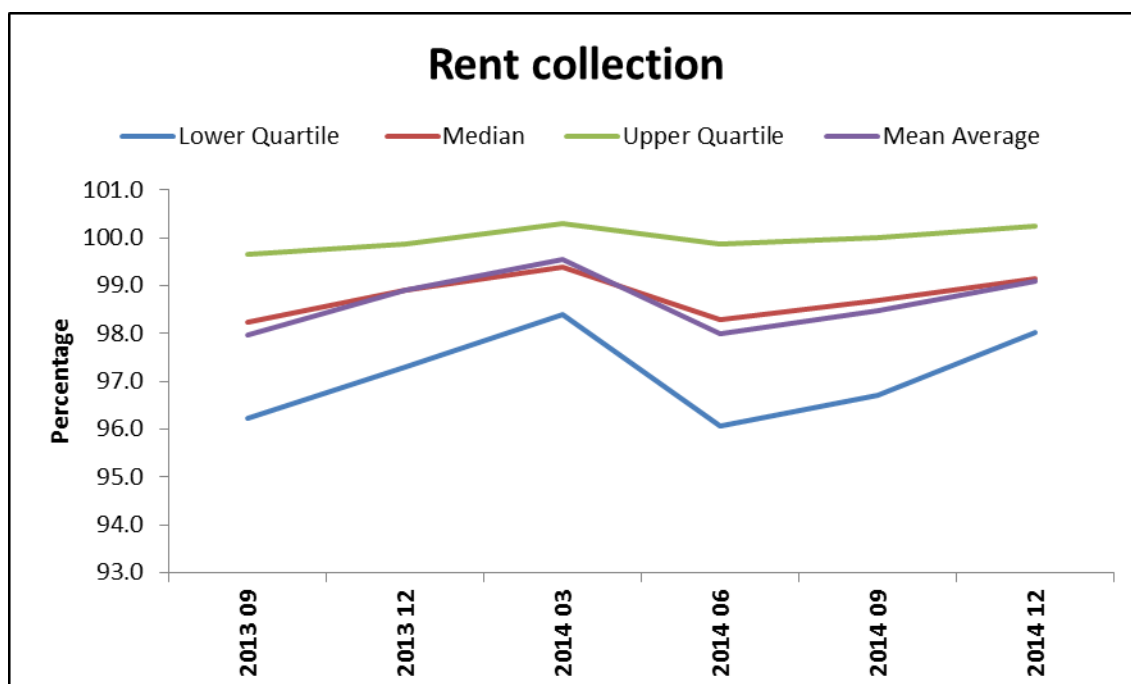
The chart below shows reported void losses; over three quarters of providers continue to report void losses of lower than 2%.



The aggregate sector void loss percentage, as reported in the latest published sector annual accounts, is 1.7%. Neither average nor median void loss percentages reported are changed from those reported last quarter at 1.6% and 1.2% respectively.

<sup>7</sup> 2013 Global Accounts of Housing Providers

Rent collection figures, presented in the graph below, show that 96% of providers report rent collection for the year to be in excess of 95%<sup>8</sup>.



Mean average and median rent collection percentages were 99.1% and 99.2% respectively (September 98.5% and 98.7%). The number of providers reporting rent collection rates of less than 95% fell to 10 (September 30).

In commenting on rent collection, a number of providers make reference to the impact of housing benefit payment cycles which do not necessarily coincide with quarter end dates. This partly explains quarterly fluctuations in rent collection rates. In the December quarter, a small number of providers also commented on a seasonal downturn in income collection over the Christmas period. However, as can be seen from the graphs, this has not had an adverse effect at sector level.

<sup>8</sup> Rent collection may exceed 100% where rents have been paid in advance or previous arrears have been recovered.

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