Homes &
Communities
Agency

Quarterly Survey for Q2 (July to September) 2017

November 2017
Homes and Communities Agency

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Introduction

This quarterly survey report is based on regulatory returns from 227 private registered providers (PRPs) and PRP groups who own or manage more than 1,000 homes.

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 July 2017 to 30 September 2017. Where any information received through the quarterly survey indicates a potential concern, this is followed up with providers.

Summary

The quarterly survey findings are:

- New finance, including refinancing, of £1.9 billion was agreed in the quarter. This came from banks and capital markets.
- The sector remains financially strong with access to sufficient finance: £15.4 billion of undrawn facilities are in place.
- Cash balances total £5.5 billion; this is forecast to reduce in the next 12 months to £4.5 billion as cash is used to fund planned capital expenditure.
- Strong operating cashflows are forecast for the 12 months ending September 2018; net operating cash flow excluding current asset sales is expected to be £6.3 billion.
- Current asset sales receipts of £599 million in the September quarter were below the £739 million forecast in June. Fixed asset sales receipts of £483 million exceeded the June forecast of £402 million for the quarter.
- In the 12 months to September 2018 the sector forecasts £3.8 billion of current asset sales and £1.7 billion of fixed asset sales.
- Investment in housing supply was £2.3 billion in the quarter to 30 September 2017; in June 2017 the forecast contractually committed spend for the quarter was £2.8 billion.
- Over the 12 month forecast period expected investment in new housing supply is £13.3 billion of which £8.9 billion is contractually committed.
- Affordable Home Ownership (AHO) activity showed a 7% quarter on quarter increase in homes developed to 2,652, a 5% increase compared to the same quarter a year ago. First tranche unit sales increased by 5% to 2,673, a 3% decrease compared to the same quarter a year ago. Taking into account transfers between tenures, there was a 3% increase in the stock of unsold units to 3,629.
- Market sale activity showed an 18% quarter on quarter decrease. A total of 897 units were sold, a 10% decrease compared to the same quarter a year ago. 932 homes were developed; there was a 3% increase in the stock of unsold properties to 1,362.

- The pipeline of expected completions in the next 18 months indicates that development activity is likely to increase. AHO completions, including committed and uncommitted development, are expected to average 4,463 per quarter (June 4,146) and market sales completions are expected to average 1,822 per quarter (June 1,768).

- Providers making use of free-standing derivatives report a reduction of 5% in the mark-to-market (MTM) exposure to £2.4 billion as swap rates increased over the quarter. In aggregate providers continue to have headroom on available collateral on MTM exposures.

- Income collection data continues to show a stable performance.

Operating environment

At a headline level the economic operating environment for PRPs remained stable in the quarter. Key metrics for the period covered include the following:

- A headline increase of 0.4% in average house prices in England for the month of September. In the year to September 2017, there was an increase of 5.4%.[1]

- In the quarter ending September 2017, output in the construction industry was estimated to have contracted by 0.9% compared with the previous quarter ending June 2017.[2]

- The Consumer Prices Index (CPI) rose by 3.0% in the year to September 2017, compared with a 2.6% rise in the year to June[3]. The rate has been increasing steadily; rates are set to remain at this level for the remainder of 2017. However, forecasters currently predict that inflation will fall to 2.4% by December 2018.[4]

- Latest estimates show that average weekly wages increased by 2.2% (not adjusted for price inflation) in the year to September 2017[5].

- Interim Construction Output Index (OPI) figures for all construction showed that costs increased by 1.8% in the year to June 2017.[6]

- The Bank of England base rate remained at 0.25% throughout the quarter. The rate increased to 0.5% in November, this was the first increase since 2007.

The survey results suggest that the sector is in a robust position to respond to any uncertainty and changes in the wider economic environment. The key risks faced by the sector are considered in the Sector Risk Profile published annually by the regulator. The 2017 update was published in July. The regulator will continue to monitor key market trends and to seek assurance that boards are actively engaged in responding to emerging risks.

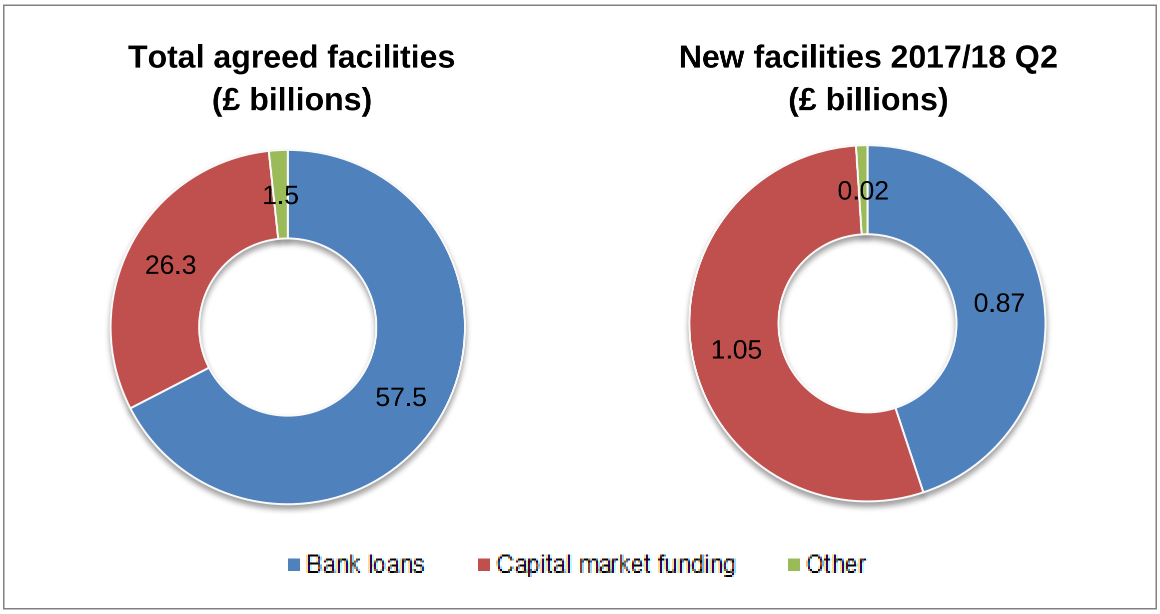
[1] UK House Price Index
[2] Construction output in Great Britain - Office for National Statistics
[3] ONS Statistical Bulletin; UK consumer price inflation: September 2017
[4] HM Treasury; Forecasts for the UK economy: a comparison of independent forecasts; October 2017
[5] UK labour market - Office for National Statistics
[6] Construction output price indices (OPIs) - Office for National Statistics

Private finance

- The sector's total agreed borrowing facilities are £85.4 billion, £57.5 billion (67%) of which are bank loans.

- New facilities, including refinancing, agreed in the quarter totalled £1.9 billion.

- Capital markets, including private placements and aggregated bond finance, contributed 54% of the new funding in the quarter; bank lending accounted for 45%; other sources, including local authority lending, contributed 1%.



- Of the £85.4 billion agreed facilities, £79.7 billion has been secured and £3.1 billion of facilities do not require security. There are further agreed facilities of £2.5 billion where security is not yet in place.

- £70.0 billion is currently drawn, leaving undrawn facilities of £15.4 billion.

- 95% (June, 96%) of providers forecast that current debt facilities are sufficient for more than 12 months.

- In the 12 months to September 2018 the sector is forecasting loan drawdowns of £7.6 billion (June 12 month forecast £7.5 billion).

- Of the 12 month forecast drawdown, £1.6 billion is from facilities not yet agreed (June £1.9 billion).

Cashflows

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[7]

Figures in £ billions	**3 months to 30 Sept 2017 (forecast)**	**3 months to 30 Sept 2017 (actual)**	**12 months to 30 Sept 2018 (forecast)**
Operating cashflows excluding sales	1.1	1.4	4.3
Interest cashflows	(0.8)	(0.8)	(3.1)
Payments to acquire and develop housing	(3.4)	(2.3)	(13.3)
Current assets sales receipts	0.7	0.6	3.8
Disposals of housing fixed assets	0.4	0.5	1.7
Other cashflows	(0.3)	0.1	(0.5)
Cashflows before resources and funding	**(2.3)**	**(0.5)**	**(7.1)**
Financed by:			
Net grants received	0.2	0.1	0.7
Net increase in debt	1.1	0.4	5.2
Use of cash reserves	1.0	0.0	1.1
Total funding cashflows[8]	**2.3**	**0.5**	**7.1**

- The sector continues to forecast strong operating cashflows. Interest cover over the 12 months to 30 September 2018, based on operating cash flows excluding sales, is projected to be 138%.

- In the 12 months to September 2018 the sector is forecasting £3.8 billion of current asset sales, of which £3.5 billion relates to properties for which development is contractually committed. In the 12 months to September 2017 current asset sales of £2.7 billion were achieved.

- In the 12 months to September 2018 the sector is forecasting £1.7 billion of fixed asset sales. In the 12 months to September 2017 fixed asset sales were £2.0 billion.

- Expenditure on new properties was £2.3 billion. This was below both the total forecast of £3.4 billion and the forecast spending of £2.8 billion on contractually committed schemes. A number of providers reported delays in their development activity.

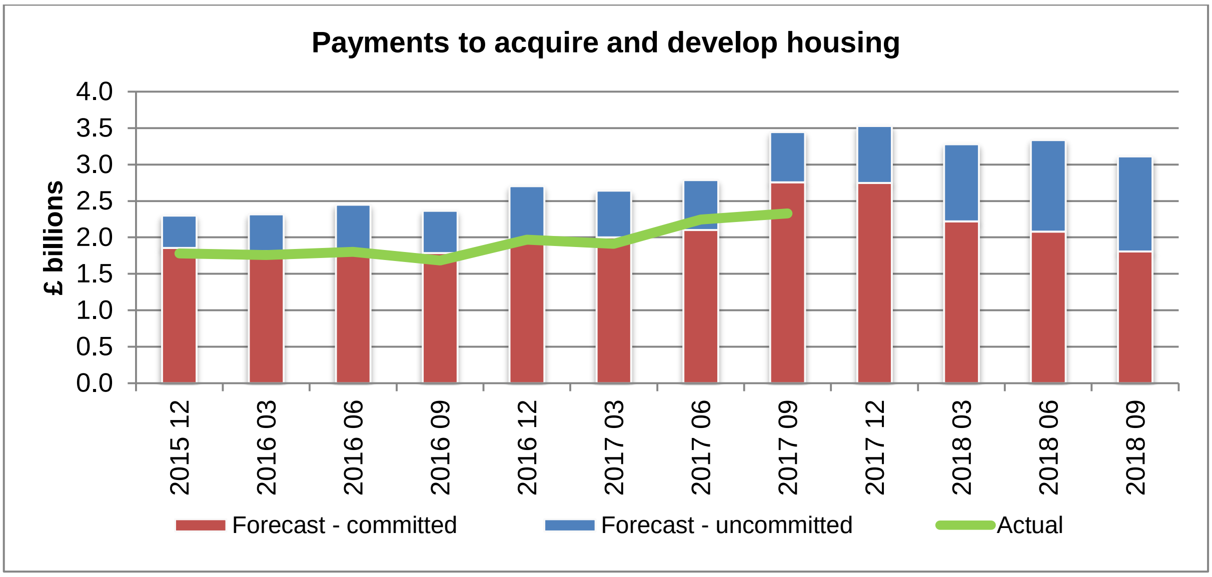
- Cash reserves used during the quarter were £37 million, compared to a forecast of £971 million. Cash available remained at £5.5 billion; this is forecast to reduce to £4.5 billion over the next 12 months as cash reserves are used to fund capital investment.

- Cash held in secured accounts at September 2017 was £755 million (June, £825 million).

[7] Operating cash flow 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.
[8] There are rounding differences in the calculated totals; figures are reported in £000

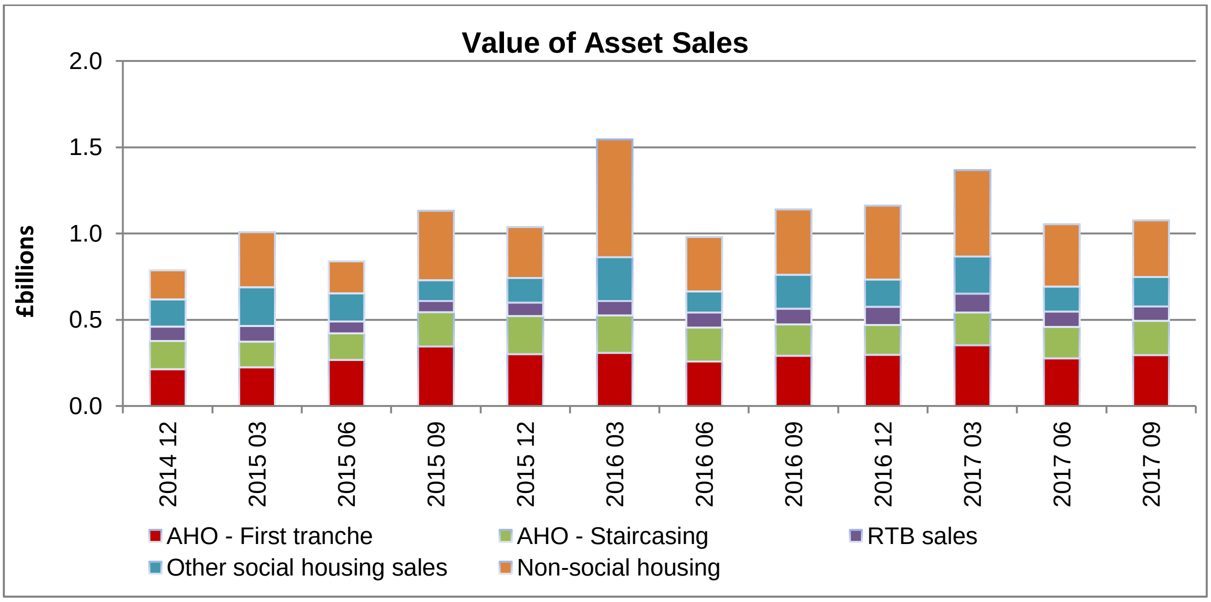
Development

In total, £8.5 billion was invested in the acquisition and development of housing in the 12 months to September 2017. Payments of £8.9 billion to acquire and develop housing properties are committed in the next 12 months; a further £4.4 billion, not contractually committed, is included in the forecasts. Actual expenditure was below forecast commitments in the current quarter.



Housing market

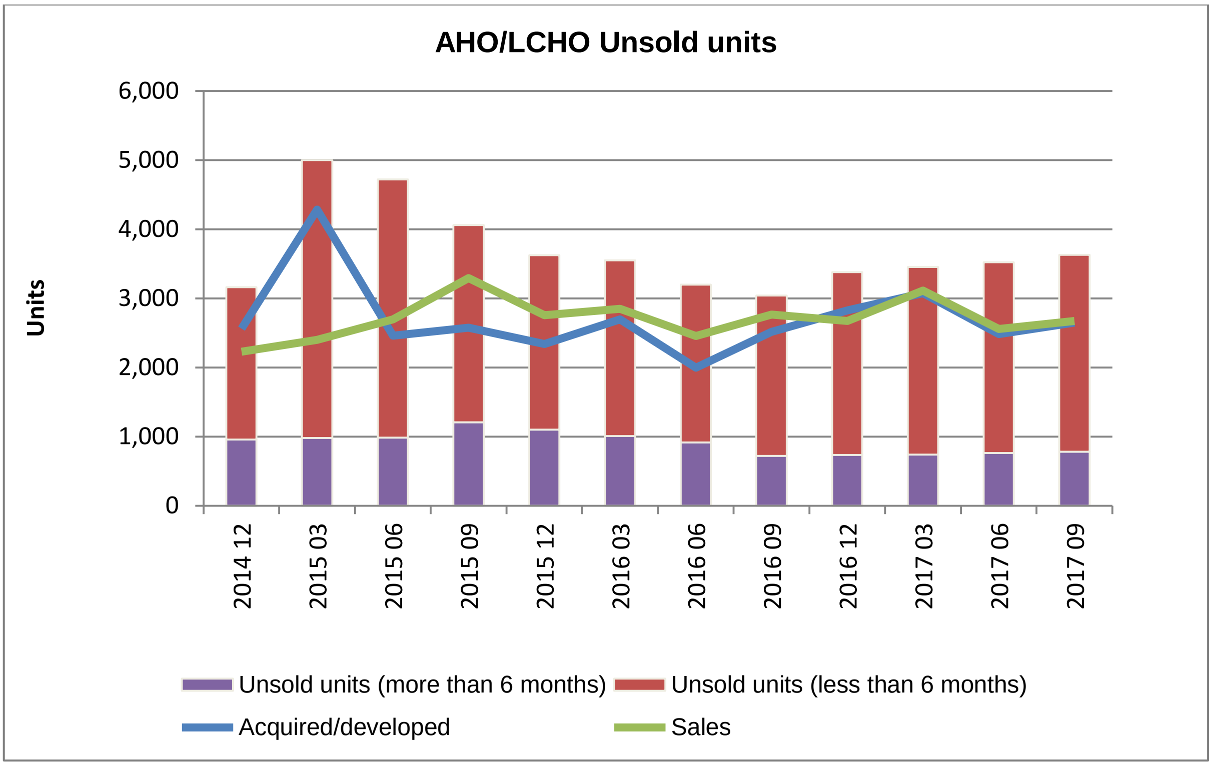
Asset sales revenue and surpluses were in line with the quarter to 30 June 2017 but slightly below the same quarter a year ago. Total asset sales of £1.1 billion generated a surplus of £405 million (June, total asset sales £1.1 billion, surplus £366 million; September 2016, total asset sales, £1.1 billion, surplus £396 million). The sales and surplus recorded in the 12 months to September 2017 was consistent with the year to September 2016.



Total asset sales in the September 2017 quarter were 5% below the forecasts received in the previous quarter. Fixed asset sales for the quarter were £483 million, above the forecast of £402 million. Current asset sales in the quarter (market sales and first tranche AHO sales) were £599 million; this was less than the forecast of £739 million.

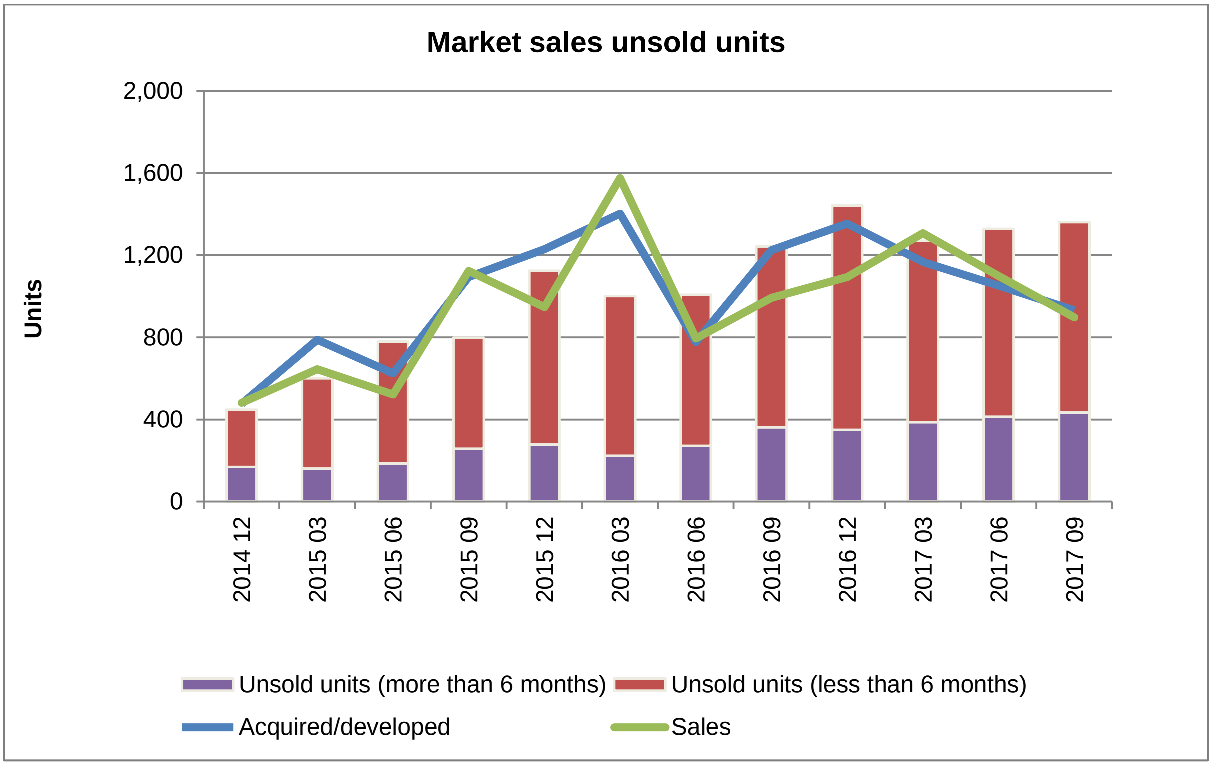
The difference between forecast and current asset housing sales achieved is concentrated in a small number of providers. Variances have been attributed to slower sales and to delays in development programmes. Where sales revenues are lower than forecast, the regulator has sought assurance that the individual providers have sufficient access to liquidity and that the delays do not have a material impact on viability. Although the providers currently remain in a strong financial position, the regulator will continue to closely monitor sales exposure.

AHO unit sales exceeded completions; there were 2,673 first tranche sales (June, 2,555) compared to 2,652 AHO completions and acquisitions (June, 2,482). However, taking into account transfers between tenures, there was a 3% increase in total unsold units in the quarter; this included a 3% increase in units unsold for over six months. At the end of September 3,629 homes were unsold (June, 3,523) of which 782 had been unsold for over six months (June, 760). Half of the unsold AHO stock at the end of the quarter was held by 20 providers.



The pipeline of AHO completions expected in the next 18 months is 26,779 (June, 24,786) of which 21,317 are contractually committed. Over the 18 months to September 2017, there were 15,544 AHO completions.

Development for outright market sale is concentrated in relatively few providers. There were 897 sales in the quarter (June, 1,099) and 932 homes were developed for market sale (June, 1,052). The number of unsold market sale units at September 2017, including transfers between tenures, increased to 1,362 (June, 1,328), of which 434 had been unsold for over six months (June, 414). For market sales, half of the total unsold stock at the end of the quarter was held by seven providers.

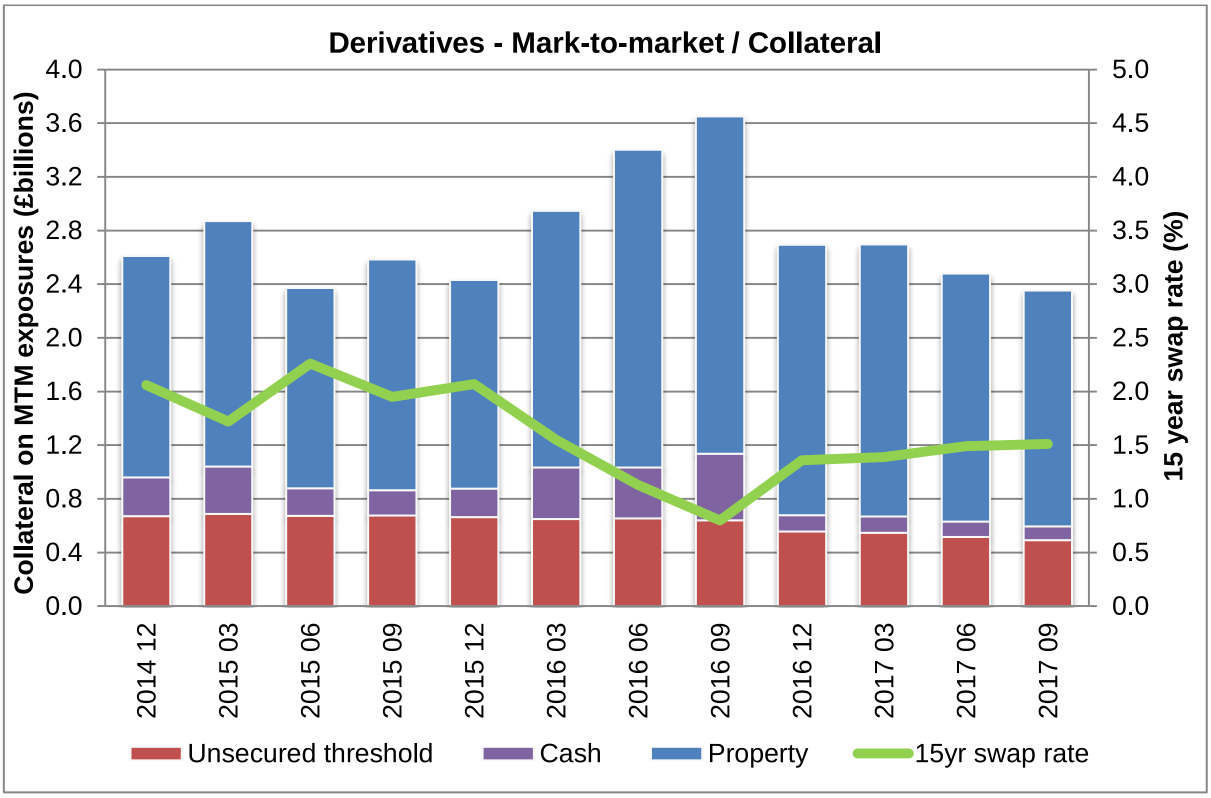


The pipeline for market sale completions expected in the next 18 months is 10,930 (June, 10,608) of which 9,351 are contractually committed. Over the 18 months to September 2017, there were 6,508 market sales completions.

Whilst there are likely to be quarterly fluctuations in the levels of for-sale development activity and sales achieved, the pipeline numbers continue to demonstrate an overall strategy of increased activity.

Derivatives

- 47 providers (June, 48) currently make use of free-standing derivatives.
- The notional value of standalone derivatives was £8.6 billion (June, £9.0 billion).
- The current gross MTM exposure was £2.4 billion (June, £2.5 billion).
- Unsecured thresholds and available security pledged to swap counterparties was £3.7 billion; of this total collateral, £2.1 billion (June, £2.2 billion) has been employed in the form of property or cash, together with unsecured thresholds of £491 million.
- The additional excess collateral available consists primarily of property pledged but not employed.



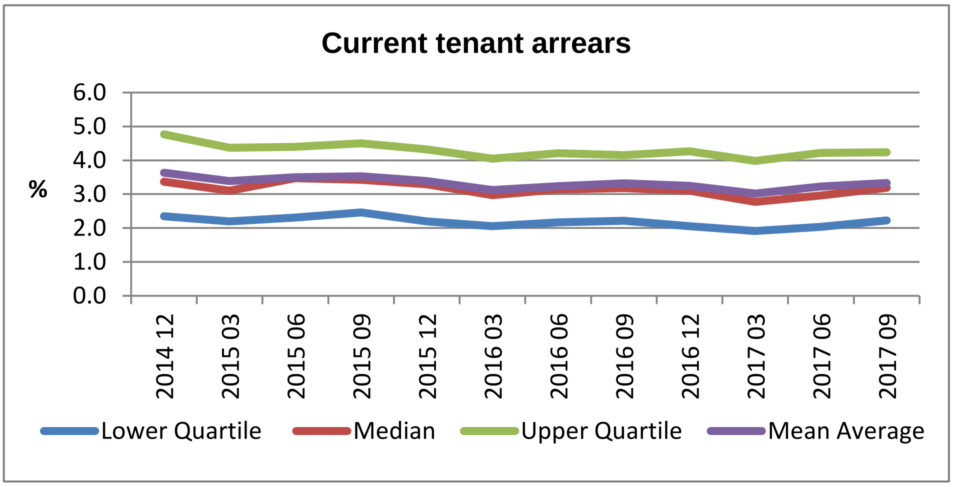
The graph above shows MTM exposures excluding excess collateral. Sterling swap rates increased over the quarter, leading to a reduction in MTM exposures.

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, headroom of collateral available over current exposure was £1.3 billion.

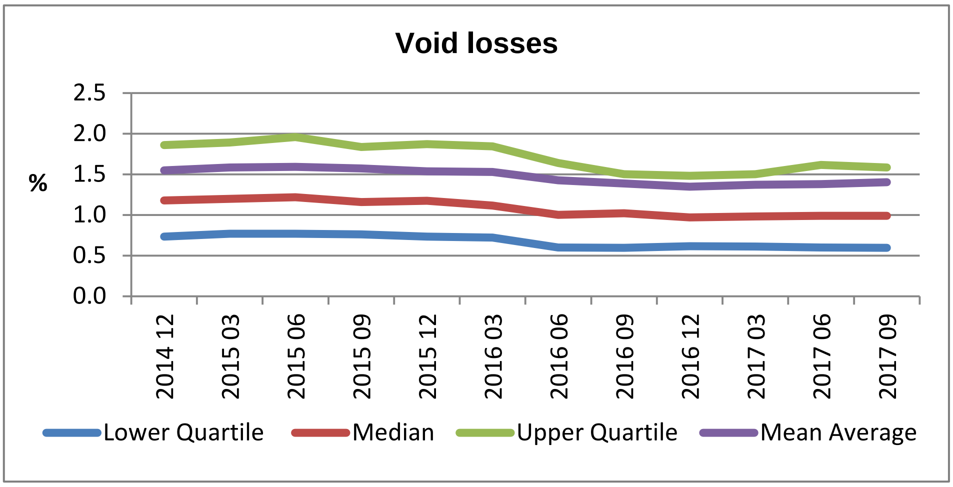
Interest rate volatility means that collateral requirements will remain a long-term exposure. Individual providers must ensure they have sufficient available security as a fall in swap rates has the potential to increase MTM exposure. The regulator will continue to monitor on-going movements in the swap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

Income collection

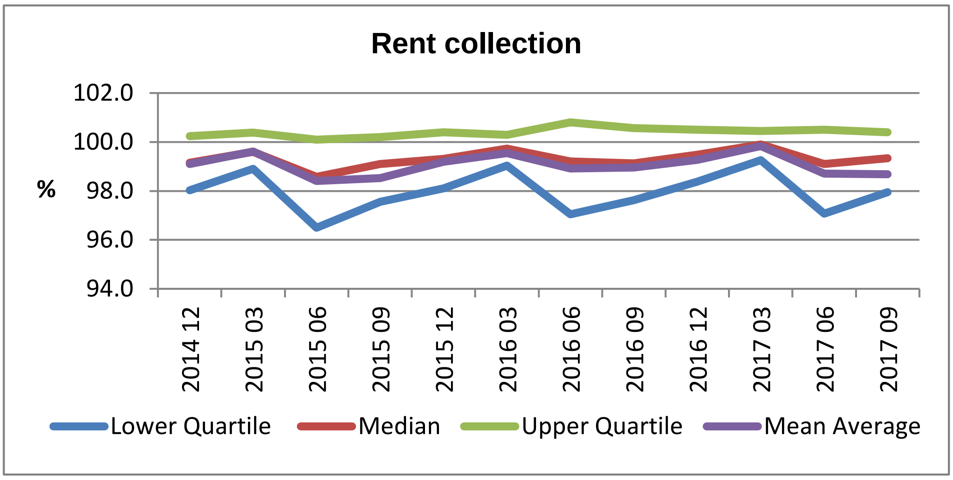
Most providers (86%) continue to report that the current levels of arrears, rent collection and voids are within, or outperforming, their business plan assumptions. The responses for each quarter remain reasonably stable, suggesting that providers are managing income collection risks and maintaining 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.



Current tenant arrears were marginally higher in the September quarter: the mean average and median were 3.3% and 3.2% respectively (June, 3.2% and 3.0% respectively).



Mean average and median void losses were unchanged from the June quarter end at 1.4% and 1.0% respectively.



Mean average and median rent collection were 98.7% and 99.3% (June, 98.7% and 99.1%).
13 providers reported rent collection rates of less than 95% (June 2017, 22; September 2016, 18).