Regulator of
Social Housing

Quarterly Survey for Q3

October to December 2017

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Introduction

This quarterly survey report is based on regulatory returns from 230 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 October 2017 to 31 December 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 of £4.1 billion was agreed in the quarter from banks and capital markets. This included an element of refinancing existing loans. Loan repayments were £948 million in the quarter.

- The sector remains financially strong with access to sufficient finance: £16.6 billion of undrawn facilities are in place.

- Cash balances total £6.0 billion; this is forecast to reduce in the next 12 months to £4.2 billion as cash is used to fund planned capital expenditure.

- Cash interest cover excluding current asset sales was 171% for the quarter. Net operating cashflows of £6.7 billion are forecast for the 12 months ending December 2018.

- Including both current and fixed asset sales, total sale receipts of £1.2 billion in the quarter were in line with the forecasts made in September.

- In the 12 months to December 2018 the sector is forecasting £5.6 billion of sales receipts. By comparison, in the 12 months to December 2017 total sales were £4.7 billion.

- Investment in housing supply was £2.8 billion in the quarter to 30 December 2017; in September 2017 the forecast contractually committed spend for the quarter was £2.7 billion.

- Over the 12-month forecast period expected investment in new housing supply is £14.0 billion of which £9.3 billion is contractually committed.

- Around 2,700 first tranche units were developed and sold in the quarter; there was no significant change in the number of unsold units. The level of development reported in the quarter to December 2017 was consistent both with the previous quarter and the same quarter a year ago.

- A total of 1,171 market sale units were sold in the quarter. This was a 31% increase on the previous quarter and a 7% increase on the same quarter a year ago. Slightly fewer units were developed in comparison to the number sold; this resulted in a small decrease in the number of properties unsold to 1,328.

- The pipeline of expected Affordable Home Ownership (AHO) completions in the next 18 months, including committed and uncommitted development, indicates delivery of an average of 4,763 homes per quarter (September 4,463); market sales completions are expected to average 1,905 per quarter (September 1,822).

- Providers making use of free-standing derivatives reported mark-to-market (MTM) exposure of £2.4 billion, a slight increase on the previous quarter reflecting a small 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.

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 December. In the year to December 2017, there was an increase of 5%.[1]

- In the quarter ending December 2017, output in the construction industry continued to contract, decreasing by 0.7% compared with the previous quarter ending September 2017.[2]

- The Consumer Prices Index (CPI) rose by 3.0% in the year to December 2017, in line with the year to September[3]. Forecasters currently predict that inflation will fall to 2.4% by December 2018.[4]

- Latest estimates show that average weekly wages increased by 2.5% (not adjusted for price inflation) in the year to December[5].

- Interim Construction Output Index (OPI) figures for all construction showed that costs increased by 2.6% in the year to December 2017.[6]

- The Bank of England base 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[7] published annually by the regulator. The regulator will continue to monitor key market trends and to seek assurance that boards are actively engaged in responding to emerging risks.

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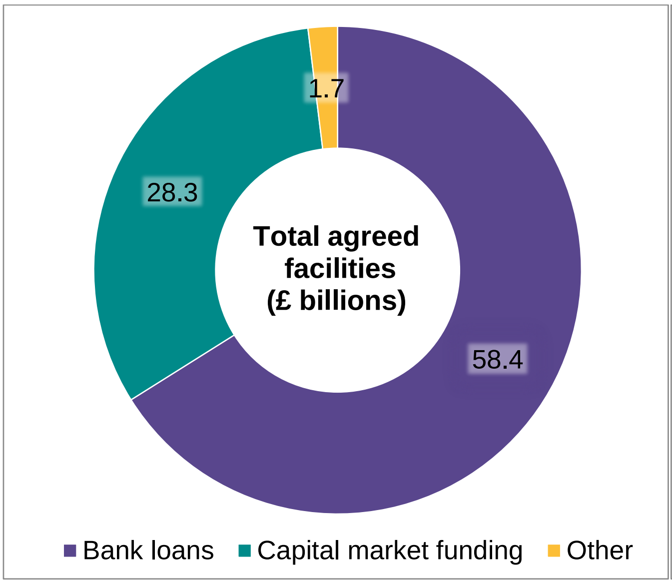
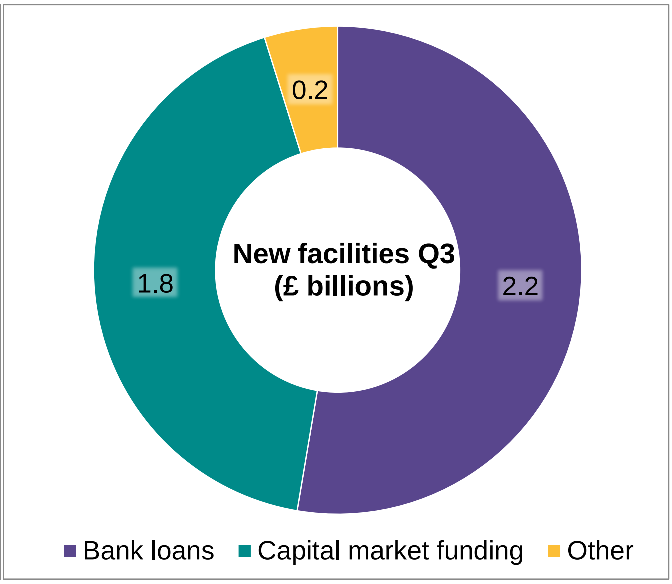
1 UK House Price Index
2 Construction output in Great Britain - Office for National Statistics
3 ONS Statistical Bulletin; UK consumer price inflation
4 HM Treasury; Forecasts for the UK economy: a comparison of independent forecasts
5 UK labour market - Office for National Statistics
6 Construction output price indices (OPIs) - Office for National Statistics
7 https://www.gov.uk/government/collections/sector-risk-profiles

Private finance

- The sector's total agreed borrowing facilities are £88.4 billion, £58.4 billion (66%) of which are bank loans.
- New facilities, including refinancing, agreed in the quarter totalled £4.1 billion.
- Bank lending accounted for 53% (£2.2 billion); this was largely in the form of revolving credit facilities (RCFs) which now account for more than 30% of all bank facilities agreed and in place.
- Capital markets funding, including private placements and aggregated bond finance, contributed 42% (£1.8 billion) of the new funding in the quarter; other sources, including local authority lending, contributed 5%.





- Of the £88.4 billion agreed facilities, £81.9 billion has been secured and £3.5 billion of facilities do not require security. There are further agreed facilities of £3.0 billion where security is not yet in place.
- £71.7 billion is currently drawn, leaving undrawn facilities of £16.6 billion.
- 95% (September, 95%) of providers forecast that current debt facilities are sufficient for more than 12 months.
- In the 12 months to December 2018 the sector is forecasting loan drawdowns of £6.4 billion (September 12-month forecast £7.6 billion).
- Of the 12-month forecast drawdown, £1.7 billion is from facilities not yet agreed (September £1.6 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[8]

Figures in £ billions	3 months to 31 Dec 2017 (forecast)	3 months to 31 Dec 2017 (actual)	12 months to 30 Dec 2018 (forecast)
Operating cashflows excluding sales	1.0	1.2	4.6
Interest cashflows	(0.7)	(0.7)	(3.1)
Payments to acquire and develop housing	(3.5)	(2.8)	(14.0)
Current assets sales receipts	0.8	0.7	3.7
Disposals of housing fixed assets	0.4	0.5	1.9
Other cashflows	(0.4)	(0.3)	(0.4)
Cashflows before resources and funding	**(2.4)**	**(1.4)**	**(7.3)**
Financed by:			
Net grants received	0.2	0.2	1.3
Net increase in debt	2.1	1.9	4.0
Use of cash reserves	0.1	(0.6)	2.0
Total funding cashflows[9]	**2.4**	**1.4**	**7.3**

- The sector continues to forecast strong operating cashflows. Interest cover over the 12 months to 31 December 2018, based on operating cash flows excluding sales, is projected to be 148%.
- Interest cover for the 3 months to 31 December 2017 was 171%; this excluded sales, development and refinancing costs and exceeded the forecast of 143%. Costs of £247 million associated with refinancing are included in other cashflows.
- In the 12 months to December 2018 the sector is forecasting £3.7 billion of current asset sales, of which £3.4 billion relates to properties for which development is contractually committed. In the 12 months to December 2017 current asset sales of £2.7 billion were achieved.
- In the 12 months to December 2018 the sector is forecasting £1.9 billion of fixed asset sales. In the 12 months to December 2017 fixed asset sales were £2.0 billion.
- Expenditure on new properties in the quarter was £2.8 billion. This was below the total forecast of £3.5 billion but above the forecast spending of £2.7 billion on contractually committed schemes.

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[8] 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.
[9] There are rounding differences in the calculated totals; figures are reported in £000

- Capitalised repair and maintenance expenditure in the quarter was £423 million. Expensed repair and maintenance expenditure is not separately identified in quarterly survey submissions and is not included in this figure. Capitalised spend was below the forecast of £535 million. Variances have been attributed to delays in repair programmes and the re-profiling of planned works.

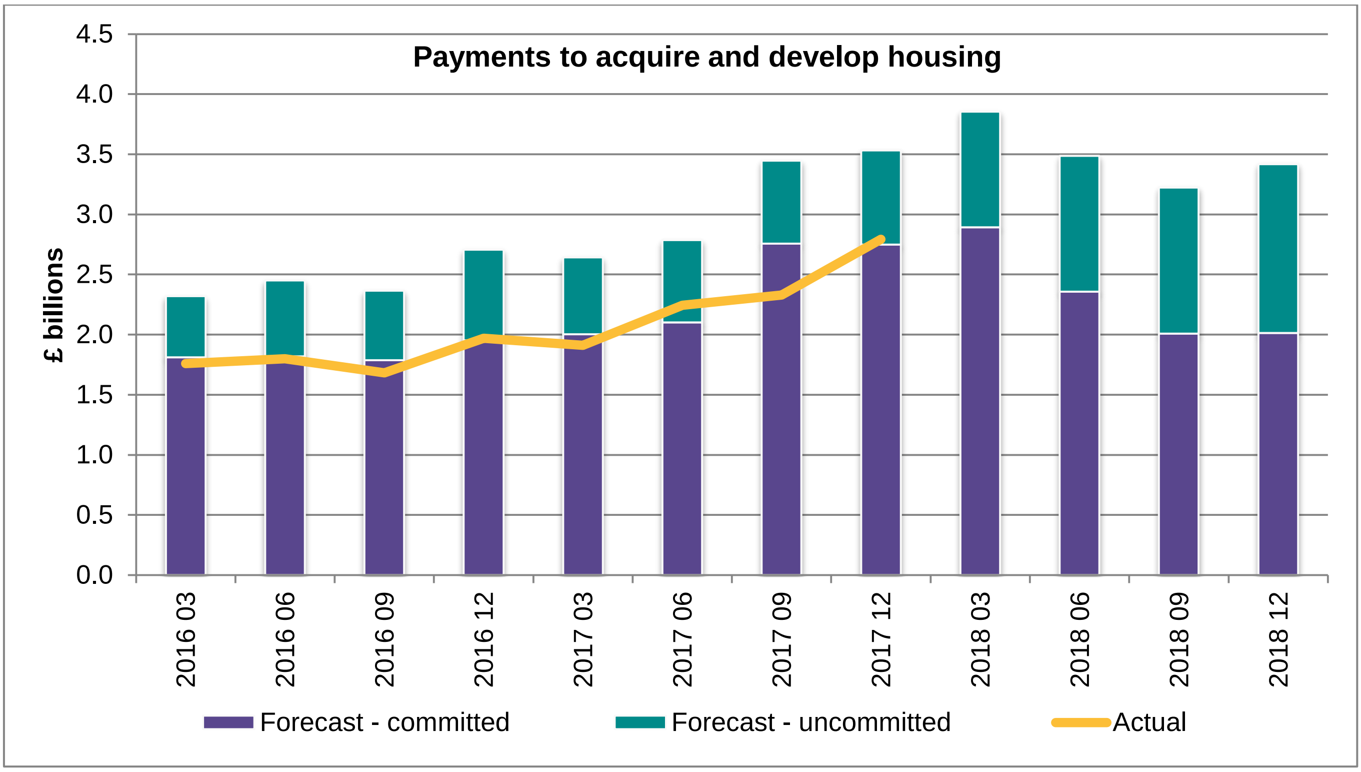
- In the 12 months to December 2017, capitalised expenditure on repairs and maintenance was £1.7 billion (previous 12 months to December 2016 £1.7bn). In the 12 months to December 2018 the sector is forecasting capitalised repairs and maintenance expenditure of £2.1 billion.

- Cash reserves increased £639 million in the quarter, compared to a decrease of £111 million as forecast in September. Cash available at December 2017 was £6.0 billion; this is forecast to reduce to £4.2 billion over the next 12 months as cash reserves are used to fund capital investment.

- In addition to the £6.0 billion available, cash held in secured accounts increased to £894 million at December 2017 (September, £755 million).

Development

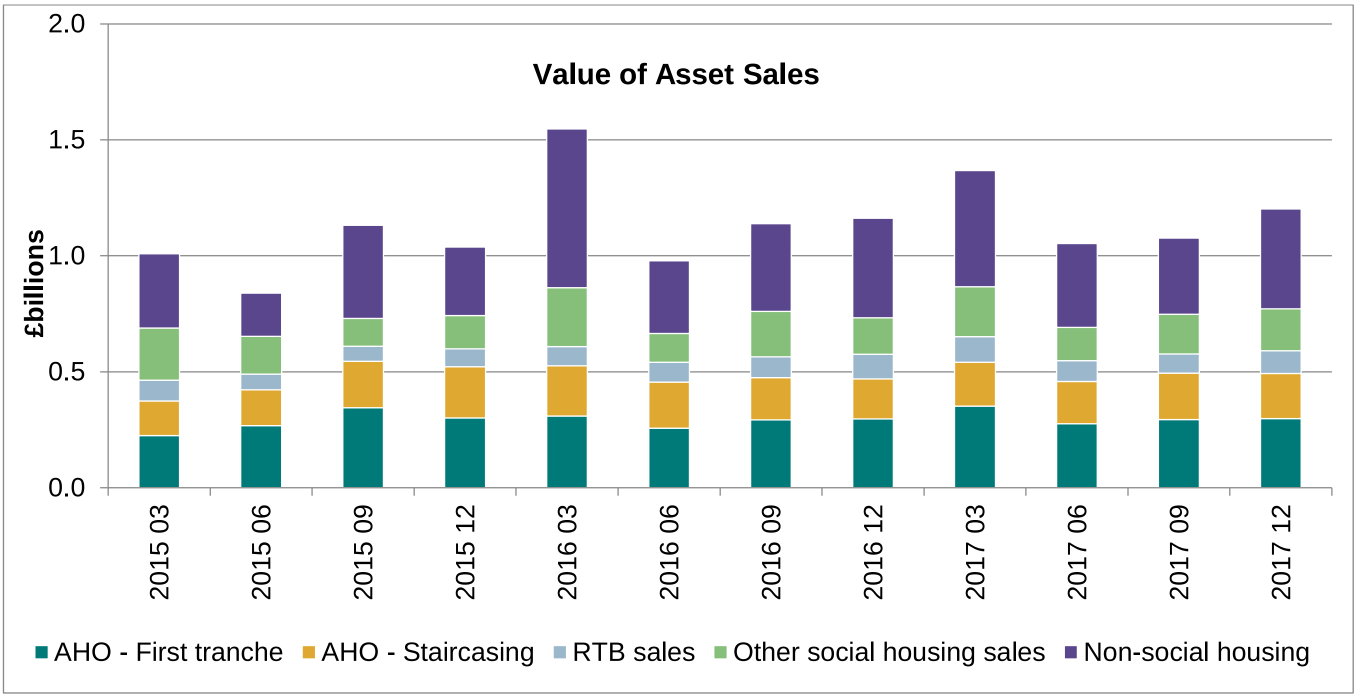
In total, £9.3 billion was invested in the acquisition and development of housing in the 12 months to December 2017. A similar amount of £9.3 billion is committed to acquire and develop housing properties in the next 12 months; a further £4.7 billion, not contractually committed, is included in the forecasts. Actual expenditure was marginally above the level of forecast commitments in the current quarter.



Housing market

Asset sales revenues of £1.2 billion increased relative to the previous quarter (quarter to 30 September 2017 £1.1billion) and were slightly greater than the same quarter a year ago. Surpluses from asset sales were £434m, an increase on £405 million for the previous quarter and higher than the surplus of £374m from the same quarter a year ago. Sales recorded in the 12 months to December 2017 were below the year to December 2016; however, the surplus achieved was higher.

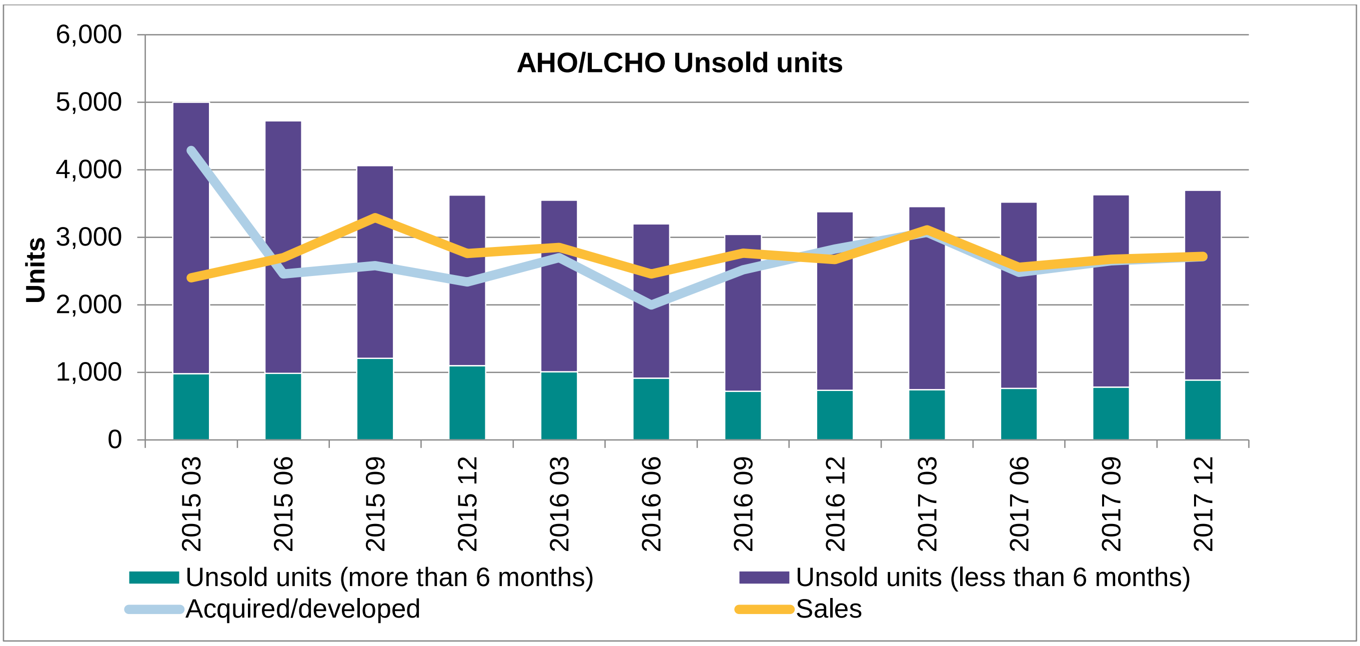
Total asset sales in the December 2017 quarter were 2% below the forecasts received in the previous quarter. Fixed asset sales for the quarter were £497 million, above the forecast of £386 million. Current asset sales in the quarter (market sales and first tranche AHO sales) were £700 million; this was less than the forecast of £834 million.



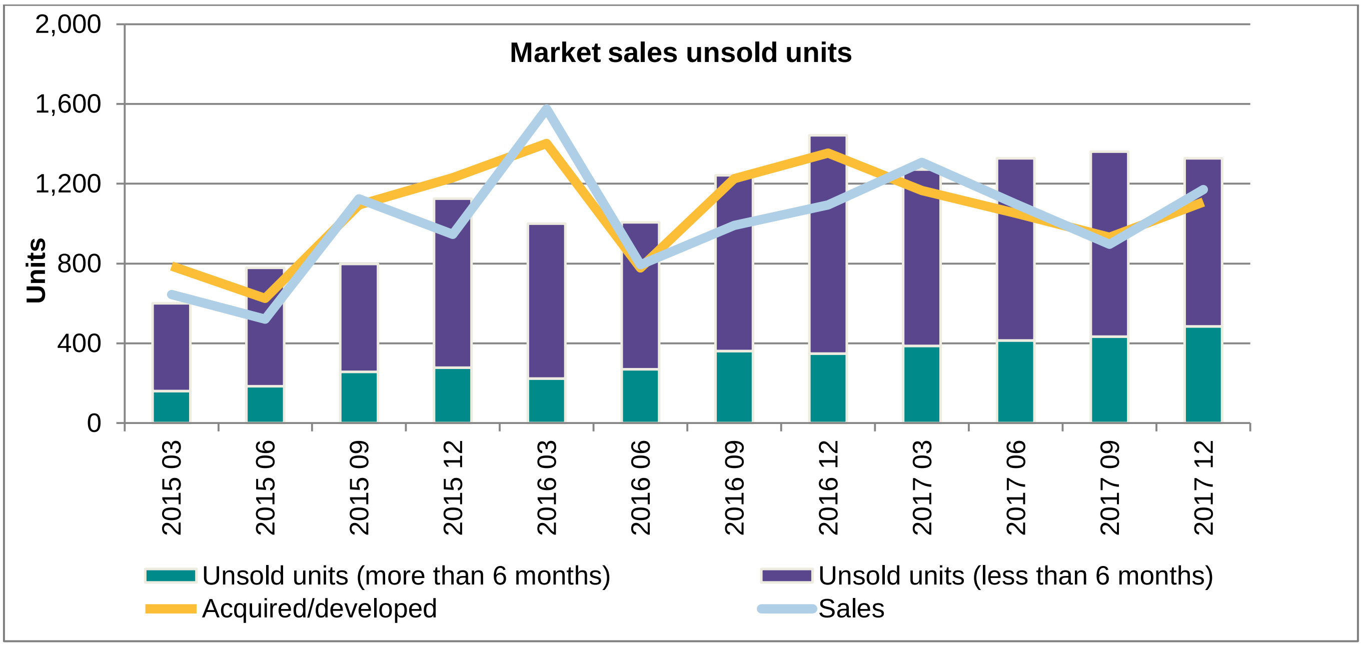
The difference between forecast and current asset housing sales achieved is concentrated in a small number of providers. Variances have been attributed to slower sales and to delays in development programmes. Where sales revenues are lower than forecast, the regulator has sought assurance that the individual 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 were broadly in line with completions; there were 2,718 first tranche sales (September, 2,673) compared to 2,712 AHO completions and acquisitions (September, 2,652). However, taking into account transfers between tenures, there was a 2% increase in total unsold units in the quarter; this included a 13% increase in units unsold for over six months. At the end of December 3,694 homes were unsold (September, 3629) of which 886 had been unsold for over six months (September, 782). Half of the unsold AHO stock at the end of the quarter was held by 21 providers.

The pipeline of AHO completions expected in the next 18 months is 28,577 (September, 26,779) of which 22,905 are contractually committed. Over the 18 months to December 2017, there were 16,261 AHO completions.



Development for outright market sale is concentrated in relatively few providers. There were 1,171 sales in the quarter (September, 897) and 1,108 homes were developed for market sale (September, 932). Taking into account transfers between tenures, the number of unsold market sale units at December 2017 decreased to 1,328 (September, 1,362), of which 485 had been unsold for over six months (September, 434). For market sales, half of the total unsold stock at the end of the quarter was held by seven providers.

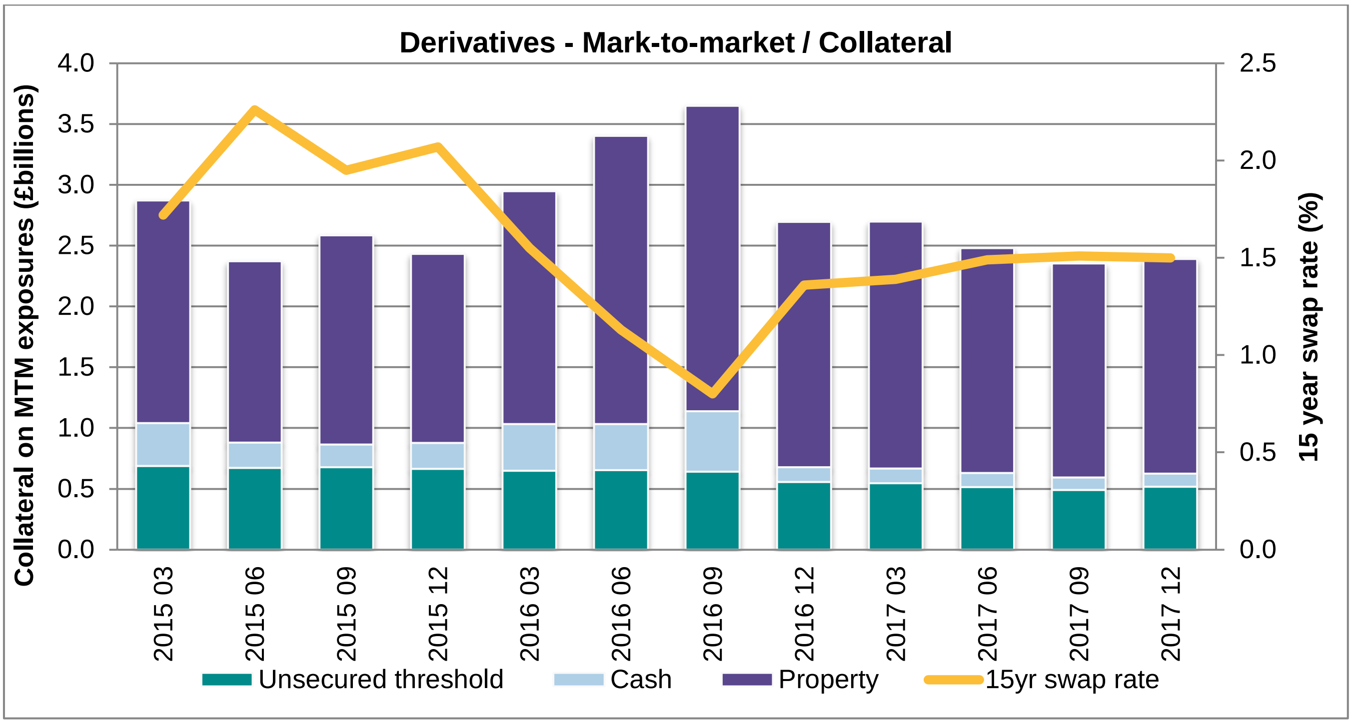


The pipeline for market sale completions expected in the next 18 months is 11,429 (September, 10,930) of which 9,783 are contractually committed. Over the 18 months to December 2017, there were 6,838 market sales completions.

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

- 46 providers (September, 47) currently make use of free-standing derivatives.
- The notional value of standalone derivatives was £8.1 billion (September, £8.6 billion).
- The current gross MTM exposure increased by 2% from September to £2.4 billion.
- Unsecured thresholds and available security pledged to swap counterparties was £3.8 billion; of this total collateral, £2.1 billion (September, £2.1 billion) has been employed in the form of property or cash, together with unsecured thresholds of £0.5 billion.
- The additional excess collateral available consists primarily of property pledged but not employed.



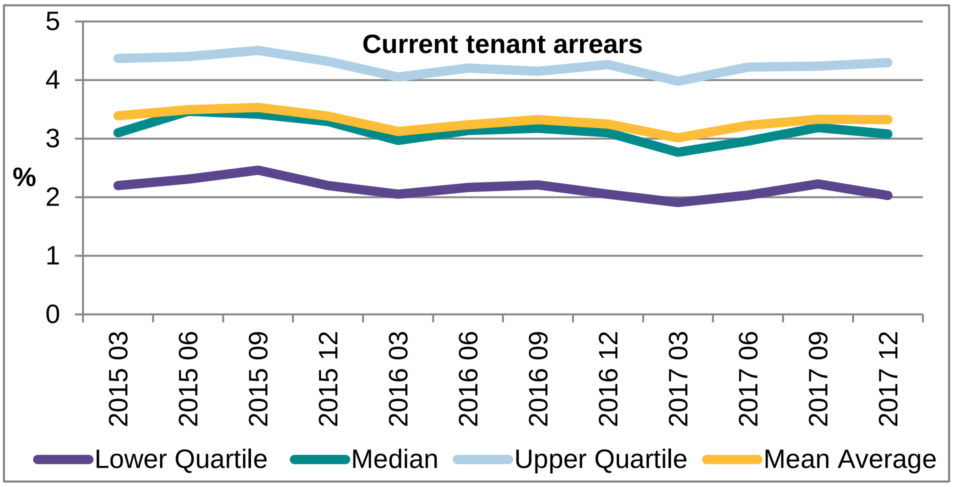
The graph above shows MTM exposures excluding excess collateral. Sterling swap rates at the end of December were marginally lower than at the end of the previous quarter. Notwithstanding the reduction in notional values, there was a slight increase in MTM exposures.

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 £1.4 billion.

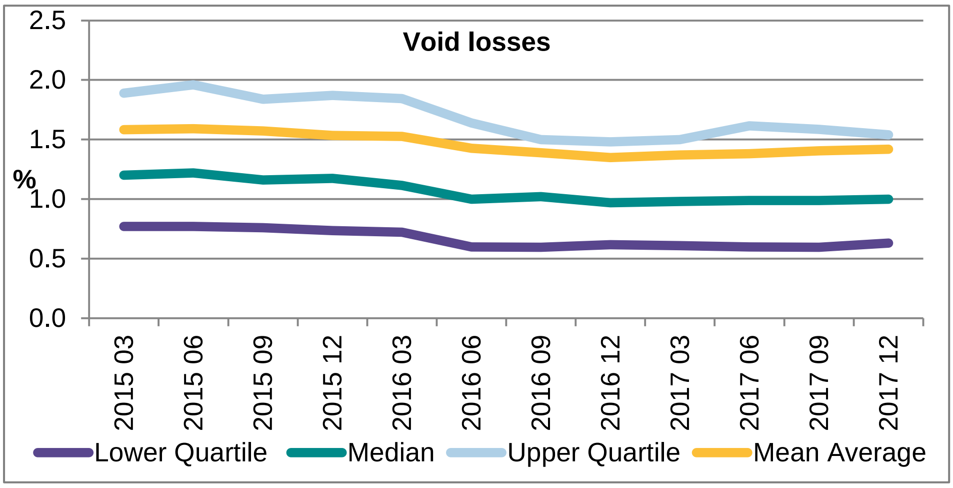
Interest rate volatility means that collateral requirements will remain a long-term exposure. Individual providers must ensure that they have sufficient available security as a fall in swap rates has the potential to increase MTM exposure. The regulator will continue to monitor on-going movements in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

Income collection

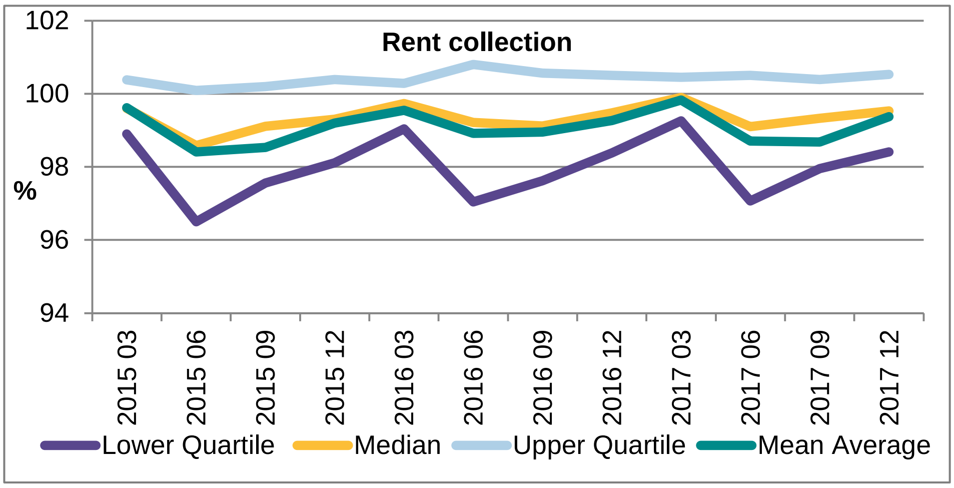
Most providers (87%) continue to report that the current levels of arrears, rent collection and voids are within, or outperforming, their business plan assumptions. The responses for each quarter remain reasonably stable, suggesting that providers are managing income collection risks and maintaining 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.



Mean average and median current tenant arrears were consistent with seasonal trends and the previous quarter at 3.3% and 3.1% respectively (September 2017 3.3% and 3.2%)



Mean average and median void losses were unchanged from September 2017 at 1.4% and 1.0% respectively.



Mean average and median rent collection were 99.4% and 99.5% (September 2017, 98.7% and 99.3%).

Eight providers reported rent collection rates of less than 95% (September 2017, 13; December 2016, 8).

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