

Quarterly survey for Q2

July to September 2018



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Introduction

This quarterly survey report is based on regulatory returns from 229 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 2018 to 30 September 2018.

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

The quarterly survey findings are:

- New finance of £2.2 billion was agreed in the quarter; £1.3 billion from banks and £0.8 billion from capital markets.
- Loan repayments were £0.5 billion in the quarter.
- The sector remains financially strong with access to sufficient finance: £18.6 billion of undrawn facilities are in place. Debt facilities now total over £90 billion.
- Cash balances total £6.6 billion; this is forecast to reduce in the next 12 months to £4.3 billion as cash is used to fund planned capital expenditure.
- Operational financial performance exceeded expectations. Cash interest cover excluding current asset sales was 165%, compared to a forecast 140% for the quarter.
- Total sale receipts of £1.3 billion in the quarter were 7% below the forecast of £1.4 billion made in June.
- In the 12 months to September 2019 the sector is forecasting £6.4 billion of sales receipts. By comparison, in the 12 months to September 2018 total sales were £5.3 billion.
- Investment in housing supply was £2.6 billion in the quarter to 30 September 2018; in June 2018 the forecasted contractually committed spend for the quarter was £3.1 billion.
- Over the 12 month forecast period expected investment in new housing supply is £15.5 billion of which £10.6 billion is contractually committed. In the 12 months to September 2018 total investment in new supply was £10.8 billion.
- Around 3,200 Affordable Home ownership (AHO) units were developed in the quarter and 3.300 were sold. There was no material change in the number of unsold units. However, the number of units unsold for more than six months was 1,400, a 39% increase on the previous quarter.

- Around 1,100 market sale units were developed in the quarter and 1,000 sold. There was a 7% increase in unsold properties. Properties unsold for more than six months increased by 33% to 757.
- Relative to current activity levels, the sector intends to increase development of for-sale properties (both AHO and market sale). In the next 18 months, including committed and uncommitted development, plans include the completion of 30,000 AHO units and 13,000 market sale properties. This compares to 17,700 AHO units and 6,500 market sale properties developed in the last 18 months.
- Providers making use of free-standing derivatives reported mark-to-market (MTM)
 exposure of £1.9 billion, a decrease on the previous quarter reflecting an increase 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.

Operating environment

In October 2018 the regulator published its annual Sector Risk Profile¹. It describes PRPs' board's role in ensuring that an effective risk management framework is adhered to. This framework should make certain that the PRP is financially viable and able to meet its social objectives in a range of different circumstances.

The publication notes that health and safety, reputational and sales risks are increasing in importance. It reflected on the need for PRPs to undertake challenging stress testing covering the crystallisation of multiple risks from a macro-economic shock or wider market downturn.

The macro-economic data for the quarter to September presents a fairly stable position. Construction industry output² grew by 2.1% in the quarter to September compared to 0.8% in the previous quarter. The Consumer Prices Index (CPI)³ rose by 2.4% in the year to September 2018 (year to June 2018: 2.4%).

However, housing market data⁴ shows a softening of the market in some areas. There was no change in the average house price in England for the month of September. Prices increased by 3.0% in the year to September 2018. London house prices fell 0.3% for the year, whilst prices in all other regions increased.

In the last six months the annual increase in average house prices has been in the range of 2.7% to 3.1%. This is the lowest level of average annual increases since 2013. Although sales registrations data for the quarter to September is not yet complete, the available information indicates that sales volumes are also lower than in recent years.

The economy is in a period of considerable uncertainty as the date of Britain's exit from the European Union nears. For the sector, this only increases the importance that PRP boards continue to demonstrate the fundamentals of sound risk management.

¹ https://www.gov.uk/government/collections/sector-risk-profiles

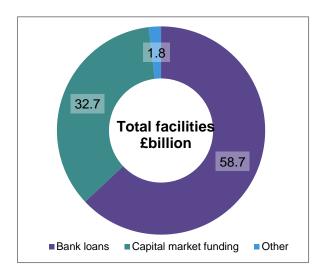
² Construction output in Great Britain - Office for National Statistics

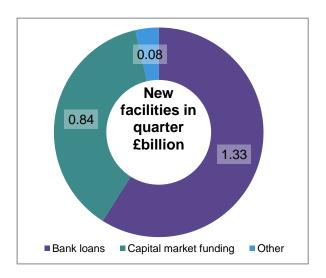
³ Consumer price inflation, UK - Office for National Statistics

⁴ UK House Price Index summary: September 2018 – Gov.uk

Private finance

- The sector's total agreed borrowing facilities are £93.1 billion, £58.7 billion (63%) of which are bank loans.
- New facilities, including refinancing, agreed in the quarter totalled £2.2 billion.
- Bank lending accounted for 59% (£1.3 billion). Capital markets funding, including private placements and aggregated bond finance, contributed 38% (£0.8 billion) of the new funding in the quarter; other sources, including local authority lending, contributed 3%.





- Of the £93.1 billion agreed facilities, £86.1 billion has been secured and £3.8 billion of facilities do not require security. There are further agreed facilities of £3.2 billion where security is not yet in place.
- £74.5 billion is currently drawn, leaving undrawn facilities of £18.6 billion.
- 93% (June, 93%) of providers forecast that current debt facilities are sufficient for more than 12 months.
- In the 12 months to September 2019 the sector is forecasting loan drawdowns of £7 billion (June 12 month forecast £6.6 billion).
- Of the 12 month forecast drawdown, £1.6 billion is from facilities not yet agreed (June £1.4 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 forecast⁵

| Figures in £ billions | 3 months to 30 Sep 2018 (forecast) | 3 months to 30 Sep 2018 (actual) | 12 months to 30 Sep 2019 (forecast) |
|---|--|--|---|
| Operating cashflows excluding sales | 1.2 | 1.3 | 4.7 |
| Interest cashflows | (0.8) | (0.8) | (3.4) |
| Payments to acquire and develop housing | (3.7) | (2.6) | (15.5) |
| Current assets sales receipts | 0.9 | 0.8 | 4.8 |
| Disposals of housing fixed assets | 0.4 | 0.5 | 1.5 |
| Other cashflows | (0.1) | (0.1) | (0.4) |
| Cashflows before resources and funding | (2.1) | (0.9) | (8.2) |
| Financed by: | | | |
| Net grants received | 0.4 | 0.2 | 1.1 |
| Net increase in debt | 1.1 | 1.3 | 4.4 |
| Use of cash reserves | 0.7 | (0.6) | 2.8 |
| Total funding cashflows ⁶ | 2.1 | 0.9 | 8.2 |

- Interest cover, based on operating cash flows excluding sales, was 165% in the quarter to September 2018. The sector continues to forecast strong operating cashflows; Interest cover over the 12 months to 30 September 2019 is projected to be 139%.
- In the 12 months to September 2019 the sector is forecasting £4.8 billion of current asset sales, of which £4.4 billion relates to properties for which development is contractually committed. In the 12 months to September 2018 current asset sales of £3.1 billion were achieved.
- In the 12 months to September 2019 the sector is forecasting £1.5 billion of fixed asset sales. In the 12 months to September 2018 fixed asset sales were £2.2 billion.
- Expenditure on new properties in the quarter was £2.6 billion. This was below the total forecast of £3.7 billion and also less than the forecast spending of £3.1 billion on contractually committed schemes.
- Capitalised repair and maintenance expenditure in the quarter was £420 million, a 9% increase on the £385 million reported in the previous quarter. This was below the forecast of £540 million. Variances have been attributed to delays in repair programmes and reprofiling of planned works.

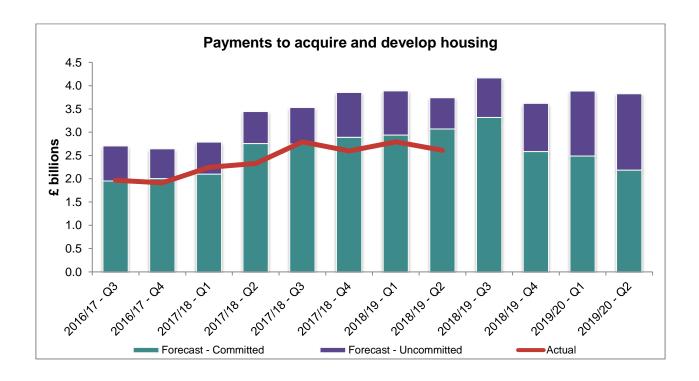
⁵ Operating cash flow excludes current asset sales receipts and costs of sales. 'Payments to acquire and develop housing properties' include payments in respect of both current and fixed assets.

⁶ There are rounding differences in the calculated totals; figures are reported in £000

- In the 12 months to September 2018, capitalised expenditure on repairs and maintenance was £1.8 billion. In the 12 months to September 2019 the sector is forecasting capitalised repairs and maintenance expenditure of £2.3 billion.
- Cash balances increased £555 million in the quarter, compared to a decrease of £718 million forecast in June.
- Cash available at September 2018 was £6.6 billion; this is forecast to reduce to £4.3 billion over the next 12 months as cash reserves are used to fund capital investment.
- In addition to the £6.6 billion available, cash held in secured accounts (and therefore not accessible to providers) totalled £1 billion at September 2018 (June, £1 billion).

Development

In total, £10.8 billion was invested in the acquisition and development of housing in the 12 months to September 2018. In the next 12 months £10.6 billion expenditure is committed to acquire and develop housing properties; a further £4.9 billion, not contractually committed is included in the forecasts.

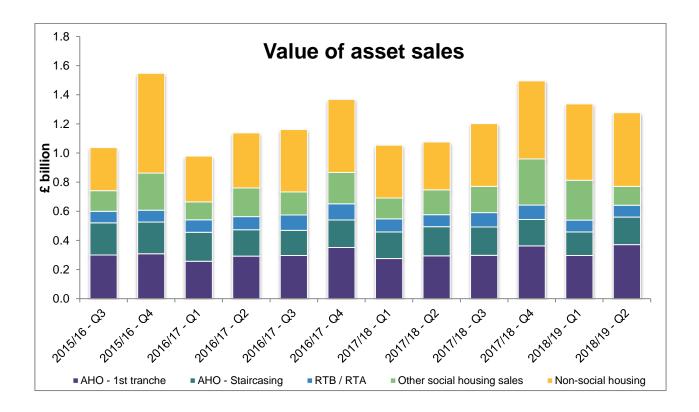


Actual expenditure in the quarter ending September 2018 was £2.6 billion. This was below both the total forecast expenditure of £3.7 billion and the £3 billion forecast on contractually committed schemes. Development programmes are subject to change and the variances are largely a result of timing differences and slippage.

Providers consistently exercise prudence in the forecasting of development cash flows by over estimating expenditures.

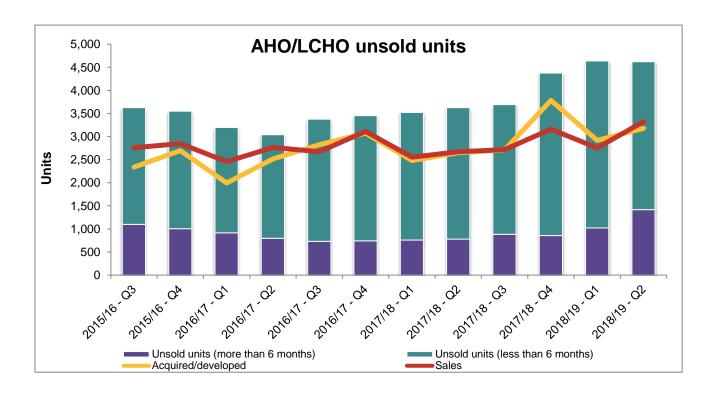
Housing market

Total sales of £1.3 billion represented a 19% increase compared to the corresponding quarter a year ago. Surpluses from asset sales were £382m, a margin on sales of 30%.



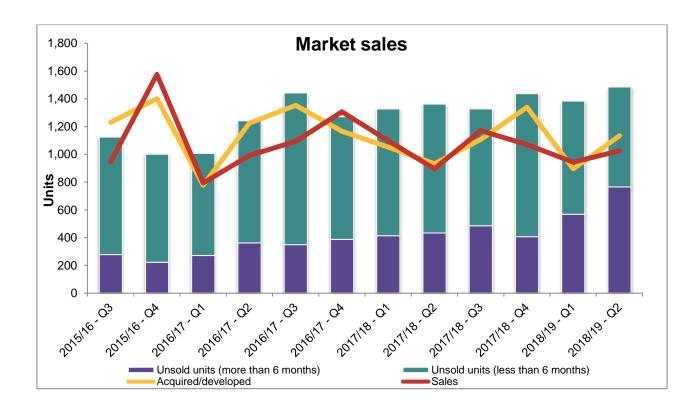
Total sales of £1.3 billion were in line with the previous quarter. Fixed asset sales for the quarter were marginally ahead of forecast at £453 million. Current asset sales in the quarter (market sales and first tranche AHO sales) were £818 million; this was less than the forecast £932 million. This 12% variance was less than the underspend on development, meaning that the lower sales have not caused a weakening of liquidity.

AHO unit sales were 3,323 (June 2,755), slightly above the 3,181 completions reported in the quarter (June 2,917). Taking into account transfers between tenures, there was no material change to the total unsold units at 4,625 (June 4,641). The number unsold for more than 6 months increased by 39% to 1,418. Half of the unsold AHO stock at the end of the quarter was held by 21 RPs.



The pipeline of AHO completions expected in the next 18 months is 30,271 (June, 28,187) of which 24,212 are contractually committed. Over the 18 months to September 2018, there were 17,731 AHO completions.

Development for outright market sale is concentrated in relatively few providers. There were 1,026 sales in the quarter (June, 944) and 1,134 homes were developed for market sale (June, 895). Taking into account transfers between tenures, the number of unsold market sale units at September 2018 increased to 1,486 (June 1,384). Of this number 757 had been unsold for over six months (June, 569). For market sales, half of the total unsold stock at the end of the quarter was held by eight providers.



The pipeline for market sale completions expected in the next 18 months is 13,273 (June, 13,260) of which 12,068 are contractually committed. Over the 18 months to September 2018, there were 6,461 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.

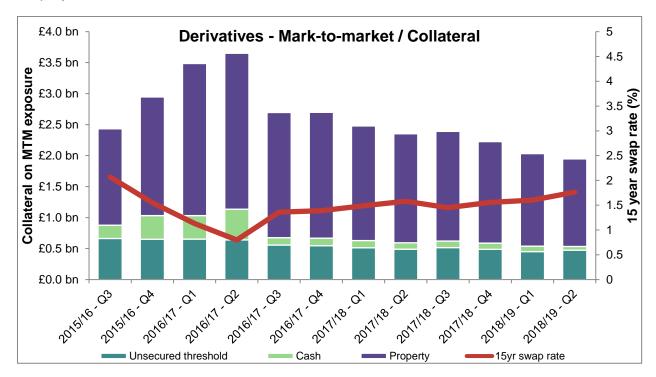
The number of properties unsold for more than six months, both low-cost home ownership and market sale, is up more than 70% compared to March 2018. This can be partly explained by a peak in delivery in the final quarter of 2017/18 when over 5,000 properties for sale were completed. This was an increase of more than 30% compared to the quarterly average for the last three years.

Some quarterly survey respondents have also reported that it is taking them a longer time to complete sales due to market conditions. This appears consistent with the economic data reported by HM Land Registry, the Bank of England and others that the housing market appears to have softened in some areas.

Whilst there are 114 PRPs with properties that have been unsold for more than 6 months, the unsold stock is concentrated: 25 providers hold 75% of the stock. The providers are well funded at present and we continue to monitor this risk on an ongoing basis.

Derivatives

- 43 providers (June, 43) currently make use of free-standing derivatives.
- The notional value of standalone derivatives was £8.5 billion (June, £8.4 billion).
- The current gross MTM exposure decreased by 4% from June to £1.9 billion.
- Unsecured thresholds and available security pledged to swap counterparties was £3.6 billion; of this total collateral, £1.6 billion (June, £1.7 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.



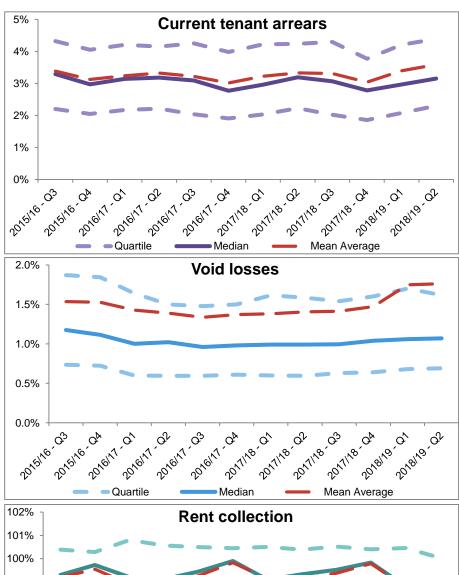
The above graph shows MTM exposures excluding excess collateral. Sterling swap rates at the end of September were higher than at the end of the previous quarter. This resulted in a decrease in MTM exposure.

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 £1.6 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 ongoing 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 cash flows 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.



Rent collection

101%

100%

99%

98%

97%

96%

95%

Quartile

Rent collection

Rent collection

Rent collection

Mean Average

Mean average and median current tenant arrears increased on the previous quarter to 3.6% and 3.2% respectively (June 3.4% and 3.0%). The median is consistent with the seasonal trend and the figures reported in September 2017. The mean average figure is impacted by additional providers added to the quarterly survey dataset in recent quarters. These providers specialise in temporary supported housing which typically has higher rates of rent arrears and void losses.

The median and quartile **void losses** were consistent with the previous quarter. Mean average void losses have increased from 1.5% in March to 1.7% in June and September. This is attributable to the additional providers added to the dataset.

Mean average **rent collection** was 98.5% whilst the median was 98.9%. Rent collection figures are also affected by the additional providers added to the dataset. Despite this results in the quarter are generally consistent with seasonal trends and housing benefit cycles. 16 providers reported rent collection rates of less than 95% (June 2018, 29 and September 2017, 12)



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or call 0300 124 5225.

or write to:

Regulator of Social Housing 1st Floor – Lateral 8 City Walk Leeds LS11 9AT

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