Regulator of Social Housing

Quarterly survey for Q3

October to December 2018

Contents

Introduction

This quarterly survey report is based on regulatory returns from 225 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 2018 to 31 December 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 £3.6 billion was agreed in the quarter; £2.1 billion from banks and £1.4 billion from capital markets.

- Loan repayments were £1.1 billion in the quarter.

- The sector remains financially strong with access to sufficient finance: £19.3 billion of undrawn facilities are in place. Debt facilities now total over £95 billion.

- Cash balances total £6.6 billion; this is forecast to reduce in the next 12 months to £4.2 billion as cash is used to fund planned capital expenditure.

- Operational financial performance exceeded expectations. Cash interest cover, excluding current asset sales, was 138% compared to a forecast of 132% for the quarter.

- Total sale receipts of £1.3 billion in the quarter were consistent with the forecast of £1.3 billion made in September.

- In the 12 months to December 2019 the sector is forecasting £6.1 billion of sales receipts. By comparison, in the 12 months to December 2018 total sales were £5.4 billion.

- Investment in housing supply was £3.3 billion in the quarter to 31 December 2018, consistent with the September forecast contractually committed spend for the quarter of £3.3 billion.

- Over the 12-month forecast period expected investment in new housing supply is £15.0 billion, of which £10.2 billion is contractually committed. In the 12 months to December 2018 total investment in new supply was £11.3 billion.

- 4,076 Affordable Home Ownership (AHO) units were developed in the quarter and 3,303 were sold. There was an 18% increase in the number of unsold units, amounting to 5,438 at the end of December.

- During the quarter the number of AHO units unsold for more than six months decreased by 5% to 1,350 at the end of December.

- 1,317 market sale units were developed in the quarter and 1,036 sold. The number of unsold properties increased by 18% to 1,755. The number of properties unsold for more than six months reduced to 697.

- The increase in the number of unsold units, both low-cost home ownership and market sale, reflects an increase in the number of units being developed. 5,393 units were acquired or developed during the quarter compared to an average of 4,051 units per quarter over the last three years.

- 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 13,100 market sale properties. This compares to 19,300 AHO units and 6,700 market sale properties developed in the last 18 months.

- Providers making use of free-standing derivatives reported mark-to-market (MTM) exposure of £2.1 billion, a £0.1 billion increase on the previous quarter 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.

Operating environment

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

- The average house price in England[1] increased by 2.3% in the year to December 2018. This is the lowest level of average annual increases since 2013. The lowest annual growth was seen in the North East, where there was a reduction in average prices of 1.0%. In London prices fell by 0.6% over the year, and in all other areas prices increased.

- The Consumer Prices Index)[2] rose by 2.1% in the year to December 2018 (year to September 2018: 2.4%). This is the lowest annual increase since January 2017, easing the pressure on costs.

- Construction Output Index figures[3] for all construction showed that costs increased by 2.7% in the year to December 2018.

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, including challenging stress testing covering the crystallisation of multiple risks from a macro-economic shock or wider market downturn.

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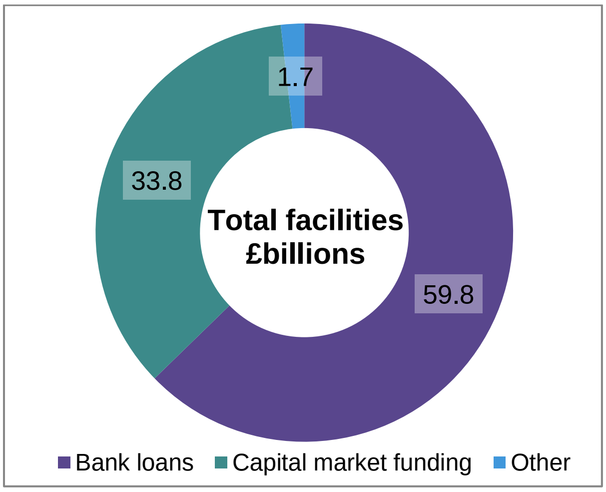
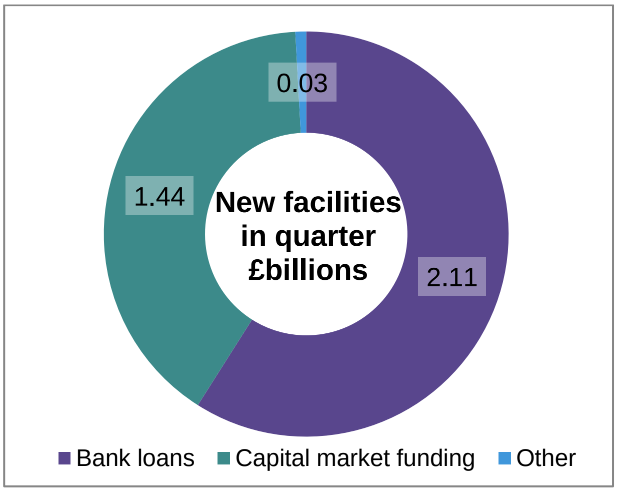
[1] UK House Price Index England – Office for National Statistics
[2] Consumer price inflation, UK – Office for National Statistics
[3] Construction output price indices – Office for National Statistics

Private finance

- The sector's total agreed borrowing facilities are £95.4 billion, £59.8 billion (63%) of which are bank loans.
- During the quarter 50 providers arranged new funding. New facilities agreed, including refinancing, totalled £3.6 billion. This compares to a mean average of £2.1 billion per quarter since April 2015. £1.1 billion worth of loans were repaid during the quarter.
- Bank lending accounted for 59% (£2.1 billion) of new funding in the quarter. Capital market funding, including private placements and aggregated bond finance, contributed 40% (£1.4 billion), and other sources, including local authority lending, contributed 1%.





- Of the £95.4 billion agreed facilities, £87.6 billion has been secured and £4.3 billion of facilities do not require security. There are further agreed facilities of £3.5 billion where security is not yet in place.
- £76.1 billion is currently drawn, leaving undrawn facilities of £19.3 billion.
- 96% (September: 93%) of providers forecast that current debt facilities are sufficient for more than 12 months.
- In the 12 months to December 2019 the sector is forecasting loan drawdowns of £7.1 billion (September 12-month forecast: £7.0 billion).
- Of the 12-month forecast drawdown, £1.2 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[4]

Figures in £ billions	3 months to 31 Dec 2018 (forecast)	3 months to 31 Dec 2018 (actual)	12 months to 31 Dec 2019 (forecast)
Operating cashflows excluding sales	1.1	1.2	4.4
Interest cashflows	(0.8)	(0.9)	(3.3)
Payments to acquire and develop housing	(4.1)	(3.3)	(15.0)
Current assets sales receipts	0.9	0.8	4.6
Disposals of housing fixed assets	0.4	0.5	1.5
Other cashflows	(0.1)	(0.2)	(0.6)
Cashflows before resources and funding	**(2.6)**	**(1.9)**	**(8.4)**
Financed by:			
Net grants received	0.3	0.3	1.2
Net increase in debt	1.0	1.6	4.5
Use of cash reserves	1.4	0.0	2.7
Total funding cashflows[5]	**2.6**	**1.9**	**8.4**

- Interest cover, based on operating cash flows excluding sales, was 138% in the quarter to December 2018 (September 2018: 165%); slightly higher than the 132% previously forecast. The reduction in interest cover compared to the previous quarter is due to increased interest costs of £0.1 billion, mainly relating to loan breakage costs, plus an increase in expenditure on capitalised repairs and maintenance of £0.1 billion. The sector continues to forecast strong operating cashflows, with interest cover over the 12 months to 31 December 2019 projected to be 132%.

- In the 12 months to December 2019 the sector is forecasting £4.6 billion of current asset sales, of which £4.2 billion relates to properties for which development is contractually committed. In the 12 months to December 2018 current asset sales of £3.1 billion were achieved.

- In the 12 months to December 2019 the sector is forecasting £1.5 billion of fixed asset sales. In the 12 months to December 2018 fixed asset sales were £2.2 billion.

- Expenditure on new properties in the quarter was £3.3 billion (previous quarter: £2.6 billion). This was below the total forecast of £4.1 billion, but in line with forecast expenditure of £3.3 billion on contractually committed schemes.

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[4] 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.

[5] There are rounding differences in the calculated totals; figures are reported in £000

- Capitalised repair and maintenance expenditure in the quarter was £0.5 billion, a 21% increase on the £0.4 billion reported in the previous quarter. This was below the forecast of £0.6 billion. Variances have been attributed to delays in repair programmes and re-profiling of planned works.

- In the 12 months to December 2018, capitalised expenditure on repairs and maintenance was £1.8 billion. In the 12 months to December 2019 the sector is forecasting capitalised repairs and maintenance expenditure of £2.3 billion.

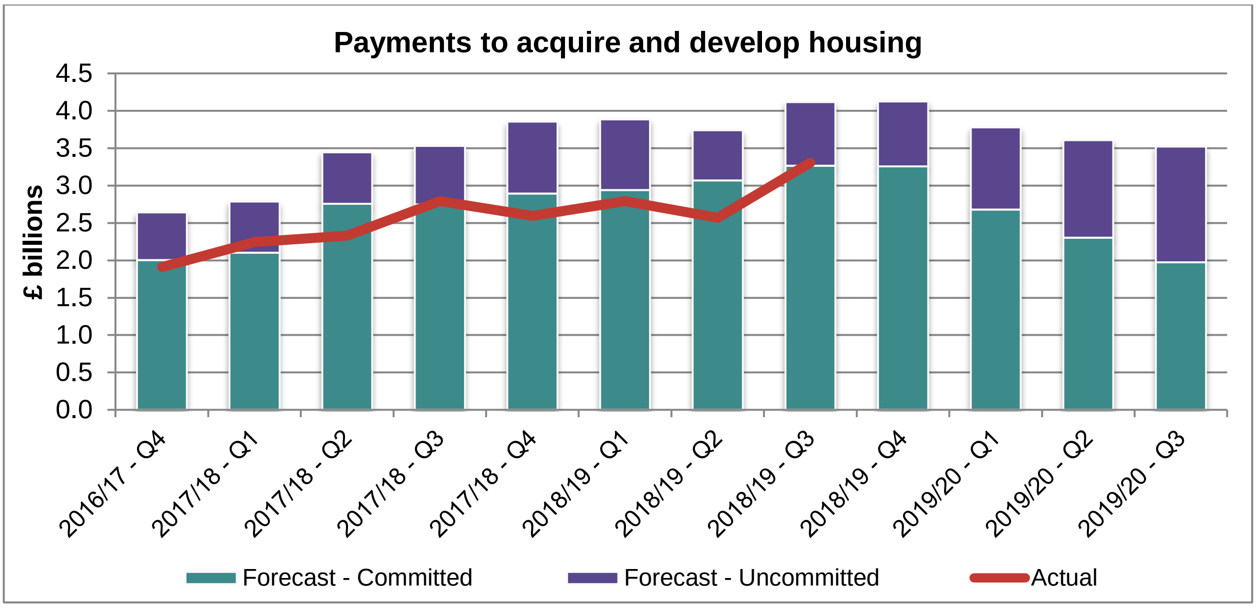
- Available cash balances increased by less than £0.1 billion in the quarter, compared to a decrease of £1.3 billion forecast in September. The main reasons for this variance were an underspend against forecast development payments of £0.8 billion and additional loan drawdowns of £0.7 billion.

- Cash available at December 2018 was £6.6 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 £6.6 billion available, cash held in secured accounts (and therefore not accessible to providers) totalled £1.0 billion at December 2018 (September: £1.0 billion).

Development

In total, £11.3 billion was invested in the acquisition and development of housing properties in the 12 months to December 2018. In the next 12 months £10.2 billion expenditure is committed to acquire and develop housing properties, and a further £4.8 billion of uncommitted expenditure has been forecast.

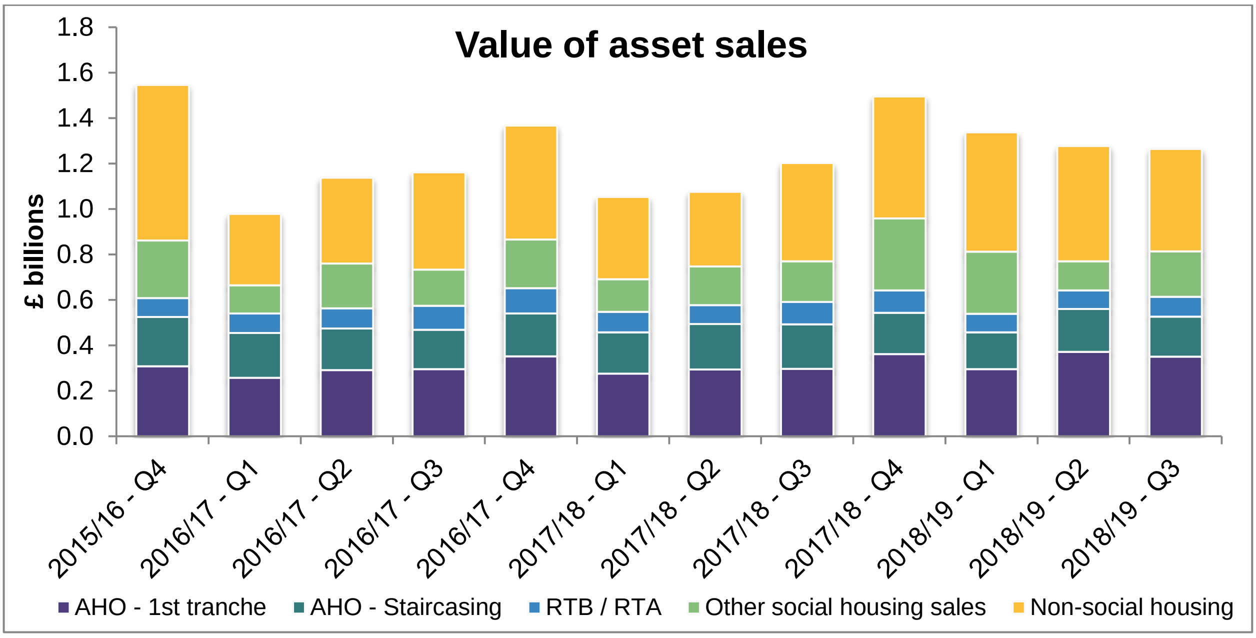


Actual expenditure in the quarter ending December 2018 was £3.3 billion, a 29% increase on the £2.6 billion reported in the previous quarter. This was below the total forecast expenditure of £4.1 billion, but in line with the £3.3 billion forecast on contractually committed schemes. Development programmes are subject to change and the variances are largely a result of timing differences and slippage.

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

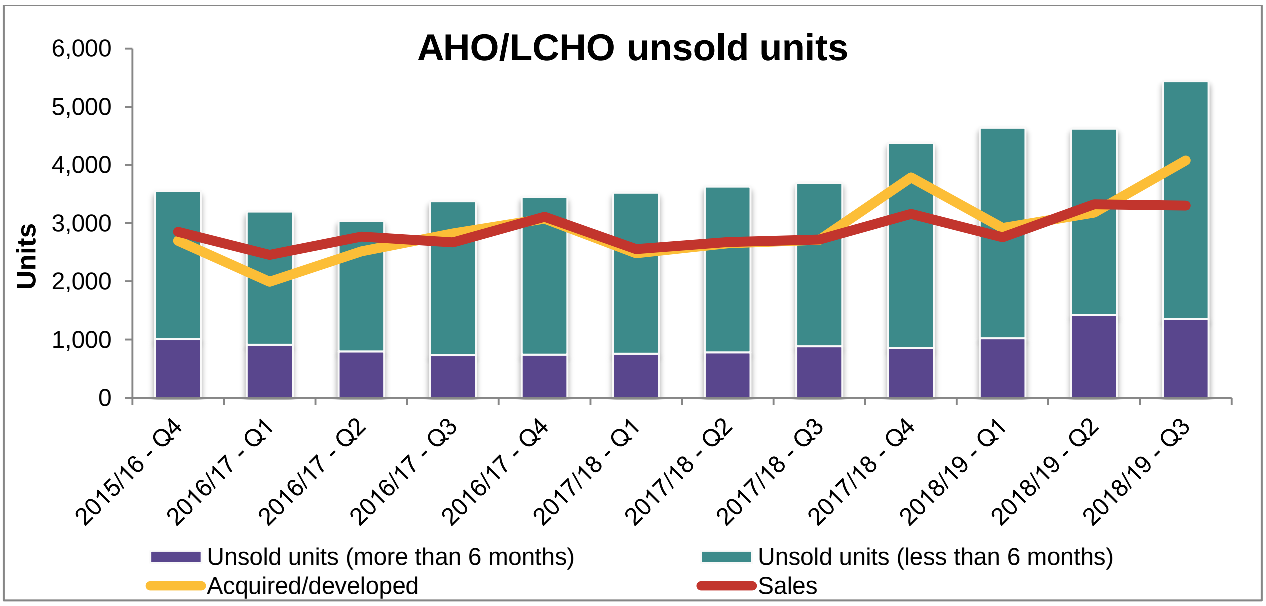
Housing market

Total sales of £1.3 billion represented a 5% increase compared to the corresponding quarter a year ago. Surpluses from asset sales were £0.3 billion, a margin on sales of 27%.



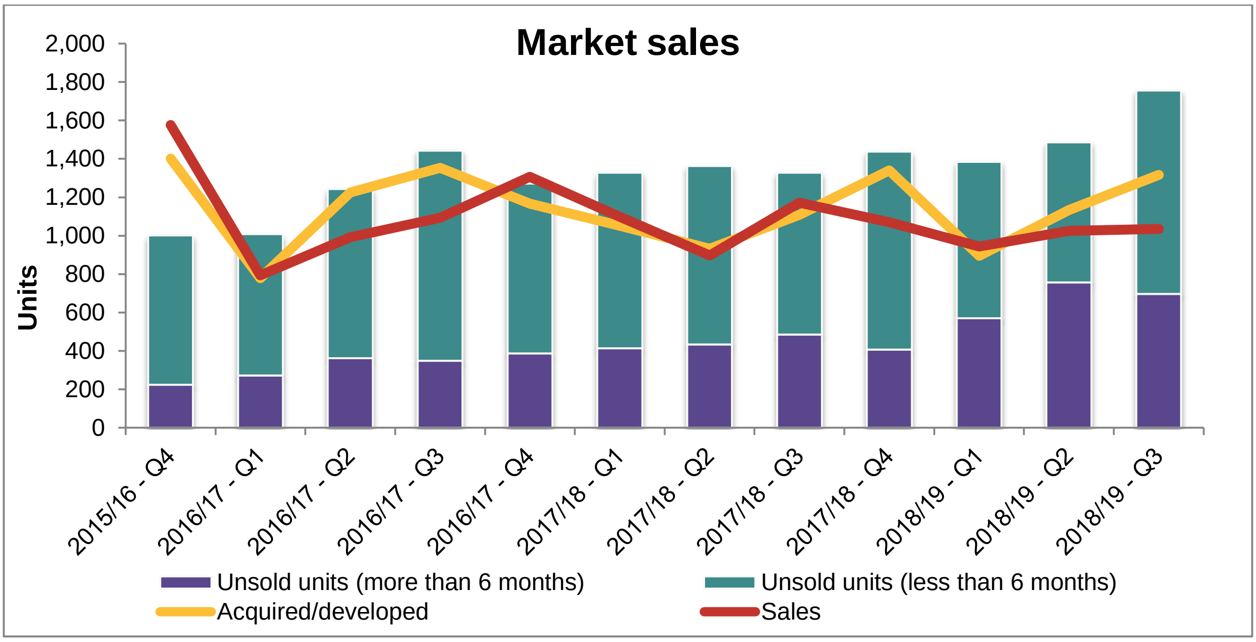
Total sales of £1.3 billion were in line with the previous quarter. Fixed asset sales for the quarter amounted to £0.5 billion; 27% higher than the £0.4 billion forecast. Current asset sales in the quarter (market sales and first tranche AHO sales) were £0.8 billion; 20% less than the forecast £0.9 billion. Expected current assets sales for the final quarter of 2018/19 have reduced from the £1.3 billion forecast in September to £1.2 billion.

AHO unit sales were 3,303 (September: 3,323) compared to the 4,076 completions reported in the quarter (September: 3,181). Taking into account transfers between tenures, there was an 18% increase in the number of unsold units, which stood at 5,438 at the end of December (September: 4,625). The number of units unsold for more than 6 months reduced by 5% to 1,350 (September: 1,418). Half of the unsold AHO stock at the end of the quarter was held by 17 RPs.



The pipeline of AHO completions expected in the next 18 months is 29,991 (September: 30,271) of which 24,845 are contractually committed. Over the 18 months to December 2018 there were 19,325 AHO completions.

Development for outright market sale is concentrated in relatively few providers. There were 1,036 sales in the quarter (September: 1,026) and 1,317 homes were developed for market sale (September: 1,134). Taking into account transfers between tenures, the number of unsold market sale units at September 2018 increased by 18% to 1,755 (September: 1,486). The number of units unsold for over six months reduced to 697 (September: 757). For market sales, half of the total unsold stock at the end of the quarter was held by six providers.



The pipeline for market sale completions expected in the next 18 months is 13,112 (September: 13,273) of which 12,210 are contractually committed. Over the 18 months to December 2018 there were 6,726 market sales completions.

Whilst there are likely to be quarterly fluctuations in the levels of market sale development activity and sales achieved, the pipeline numbers continue to demonstrate an overall strategy of increased activity, with planned completions over the next 18 months being 95% higher than the number of units delivered over the previous 18 months.

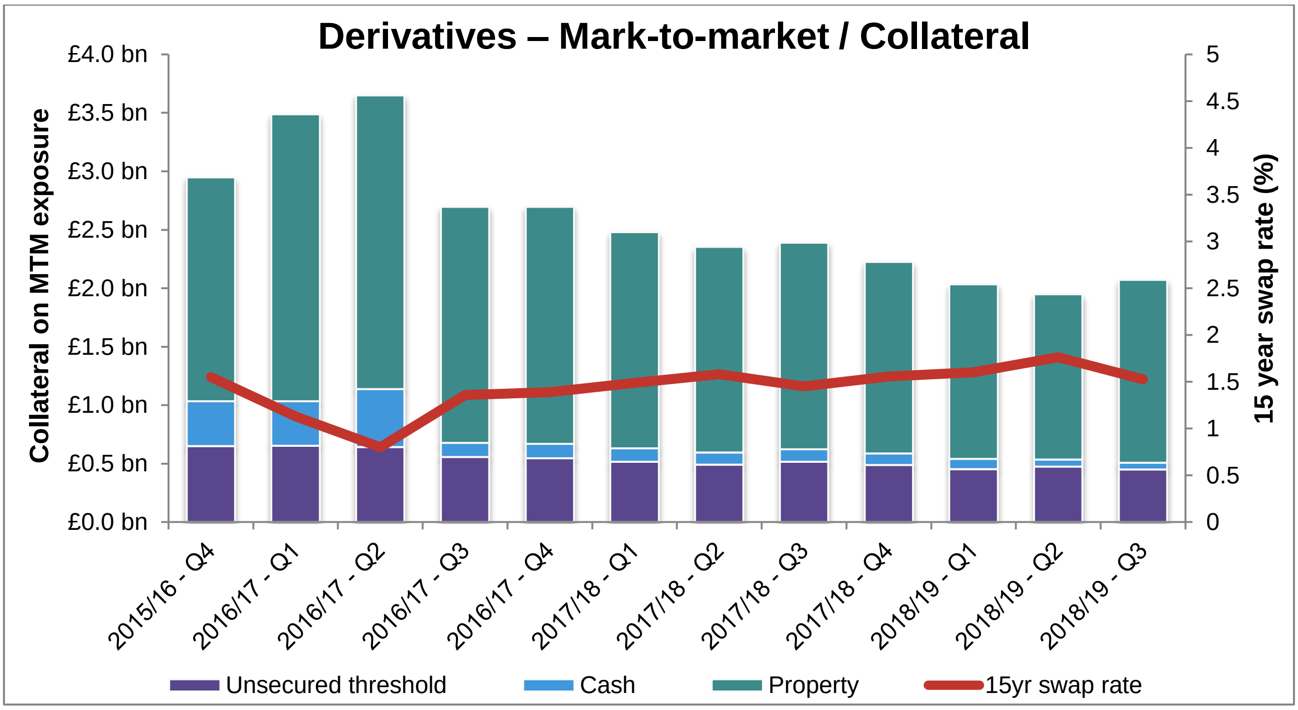
The overall number of unsold properties, both low-cost home ownership and market sale, has risen by 18% to 7,193 in the quarter ending December 2018, an increase of 1,082 units. This reflects an increase in the number of units being developed; 5,393 units were acquired or developed during the quarter compared to an average of 4,051 units per quarter over the last three years. Although there has been an increase in the overall number of unsold units, the number of units unsold for more than six months has reduced by 6% to 2,047 units.

Unsold units are concentrated in relatively few providers, operating mainly in London and the South East[6]. The providers are well funded at present and we continue to monitor this risk on an ongoing basis.

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

Derivatives

- 43 providers (September: 43) currently make use of free-standing derivatives.
- The notional value of standalone derivatives was £8.5 billion (September: £8.5 billion).
- The current gross MTM exposure increased by 6% from September to £2.1 billion.
- Unsecured thresholds and available security pledged to swap counterparties was £3.5 billion. Of this total collateral, £1.7 billion (September: £1.6 billion) had 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.



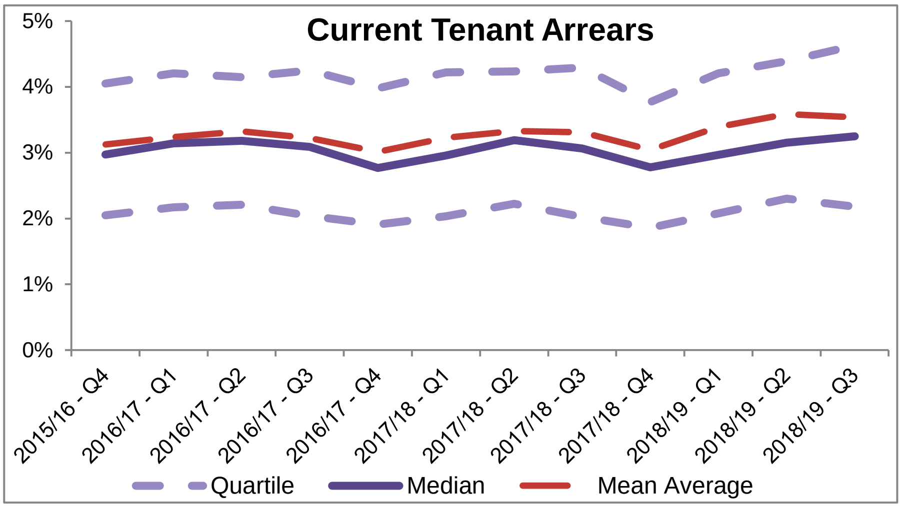
The above graph shows MTM exposures excluding excess collateral. Sterling swap rates at the end of December were lower than at the end of the previous quarter, resulting in an increase in MTM exposure.

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 £1.4 billion.

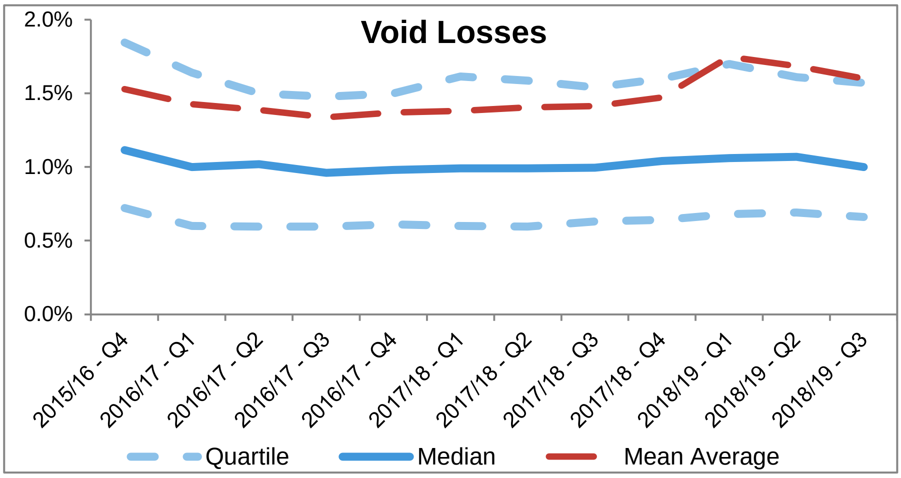
Interest rate volatility means that collateral requirements will remain a long-term exposure. Individual providers must ensure that they have sufficient available security as a fall in swap rates has the potential to increase MTM exposure. The regulator will continue to monitor ongoing movements in the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

Income collection

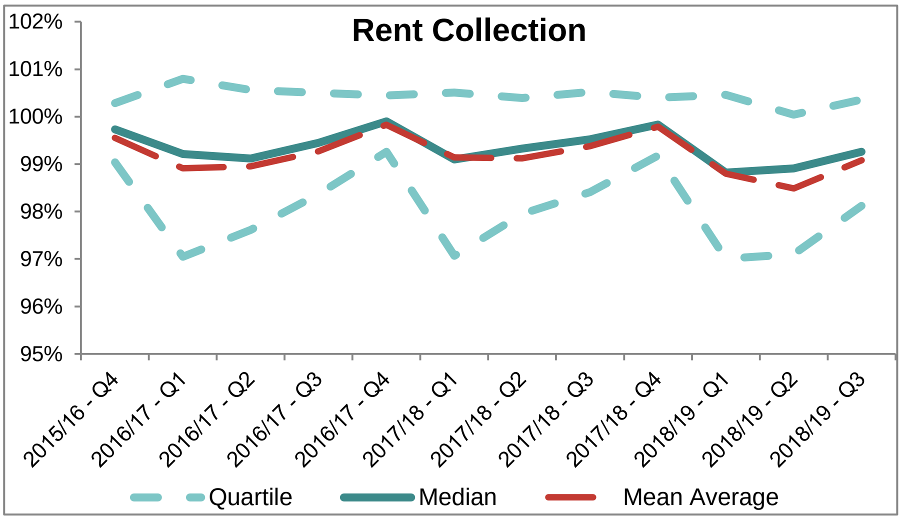
Most providers (86%) continue to report that the current levels of arrears, rent collection and voids are within, or outperforming, their business plan assumptions. The responses for each quarter remain reasonably stable, suggesting that providers are managing income collection risks and maintaining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



Median current tenant arrears increased during the quarter to 3.3% (September: 3.2%). The mean average reduced to 3.5% (September: 3.6%). Median arrears are slightly higher than the seasonal trend, which has been 3.1% in both December 2017 and 2016.



Mean and median void losses both reduced during the quarter to 1.6% and 1.0% respectively (September: 1.7% and 1.1%). There are 12 providers with void losses of over 5%, which, if excluded from the dataset, reduce the mean average down to 1.2%.



Mean average rent collection was 99.1% whilst the median was 99.3%. Median rent collection rates are slightly lower than the seasonal average, which was 99.5% in both December 2017 and 2016. Nine providers reported rent collection rates of less than 95% (September 2018: 16 and December 2017: 8).

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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.