Narrative and Examples of Financialisation & Institutionalisation of Affordable Housing

Briefing Paper

September 2019

Executive Summary

Topic of Briefing: Narrative and Examples of Financialisation & Institutionalisation of Affordable Housing

Written for: UCL's Bartlett School of Construction and Project Management's (BSCPM) one-day conference "The Case of Affordable Housing: a global perspective on financing and institutional ownership" Round Table Discussion "Tackling the housing crisis-councils, housing associations and Homes England" (12th September 2019)

Conclusion: Financing and institutional ownership of affordable housing is a sustainable way to provide sub-market housing to the people who need it most. As opposed to making private market housing affordable through demand-side interventions, institutional affordable housing aims to create a fully functional market of its own by utilising its key strengths: long term asset value and long-term rental income streams.

Housing organisations and akin agencies make institutional ownership of affordable housing successful by utilising these key strengths to maintain or deliver more services. Historically, rental income streams allowed these organisations to cycle funding back into stock and services and together with their own asset base (their housing stock), to borrow finance to build more housing. Today, these rental streams and long-term asset value are sufficiently attractive that they are being utilised as sources for significant investment.

Confidence in this market is underpinned by a regulatory regime that has been in various forms for over 45 years.

The Conference & Round Table Discussion

The purpose of the conference was to:

"*Bring together academics and a wide range of industry stakeholders to explore global case studies focused on new tools and models for financing affordable housing, working towards viable solutions for the UK and beyond*"

Aquila Chief Executive Steve Douglas joined the following for the round table discussion "Tackling the housing crisis - councils, housing associations and Homes England:

- Paul Hackett, CEO Optivo, Honorary Professor at BSCPM, UCL
- Colm Lacey, Brick by Brick
- Helen Evans, Network Homes and Chair of the G15
- Harry Swales (On behalf of Nick Walkley), Homes England

Other topics presented on the day included:

- Role of the state in affordability
- Role of mortgage market in affordability
- Land value capture
- Impact on policies (rent regulation and Help to Buy) on investment
- Has affordability improved?
- Supply Chains to increase delivery
- Global perspectives on affordable housing

Terminology

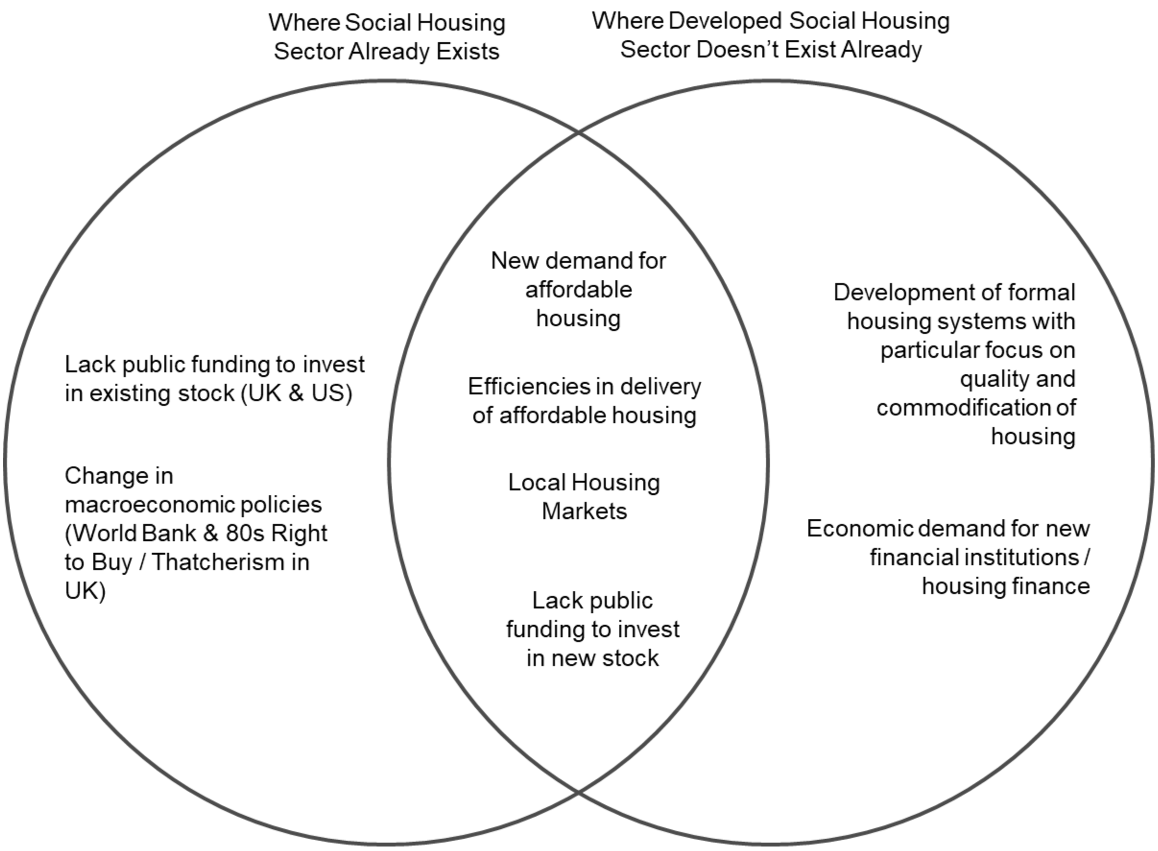
Affordable Housing: The conference referred to affordable housing generally and considers affordable housing to be a literal definition, i.e. housing that is affordable to the local population. In this briefing paper, we will use this definition for affordable housing, and will specify where social housing systems exist as products of sub-market interventions.

Institutional Ownership: The conference referred to institutional ownership as represented by affordable housing providers that build and manage affordable housing for rent and sale at sub-market levels. In this briefing paper, institutional ownership refers to state and non-state and profit and not-for-profit organisations. For the purposes of this briefing paper, institutional ownership does not include housing offered in the private rental sector by private landlords.

Part 1: Drivers for Financing Affordable Housing

Drivers for financialisation and institutionalisation of affordable housing are most clearly different between jurisdictions that *already have social housing systems* and jurisdictions that *do not have such systems*. These drivers are outlined in the figure below.

Figure 1: Venn Diagram of drivers for financialisation and institutionalisation of affordable housing



1. Where Social Housing Sector Already Exists: Driven by lack of public funding and adjacent policy change and usually in developed countries, jurisdictions where social housing systems already exist can be further divided into:
   - **Those that move away from institutional ownership of sub-market/social housing altogether (such as the USA).**
     - The Section 8 series of programmes in the USA pay the majority of rent for 2.1 million households (c. 1.6% of population) but the programme is based on budget available to the HUD (U.S. Department of Housing and Urban Development) and is not provided as a statutory welfare benefit. This means many people are on waiting lists to receive vouchers, and often will earn an income high enough to exclude them from the programme before a voucher is offered to them. It is decentralised and offered by authority-level housing agencies (i.e. at the city

level) and levels of payment vary by area. There are two pain programmes as part of Section 8:

- The Housing Choice Voucher Programme provides "tenant-based" rental assistance, so a tenant can move from a home of at least minimum housing quality to another. It also allows individuals to apply their monthly voucher towards the purchase of a home. This is an indirect subsidy to the private market.
- The programme also authorizes a variety of "project-based" rental assistance programmes, under which the owner reserves some or all of the homes in a building for low-income tenants, in return for a federal government guarantee to make up the difference between the tenant's contribution and the rent in the owner's contract with the government. This is a direct subsidy to private landlords.

- **Those that embrace institutional ownership of sub-market/social housing but look to alternative financing due to insufficient public spend on the capital cost of housing (such as the UK). These include housing associations, local authorities and for-profit private providers of affordable housing.**

Learning for the conference is generally focused on the latter, but the former illustrates what happens when jurisdictions reject financialisation and institutional ownership of affordable housing systems entirely (see Note 1).

Note 1:

Driven also by lack of funding or insufficient and adjacent policies, some jurisdictions move away from institutional ownership of sub-market/social housing and may reject institutions almost entirely, instead targeting housing policies on subsidies for first time homebuyers and subsidised rental in the private sector. The move away from Public Housing in the US is an example. Driven by alternative housing policies, such as quality of stock, economic improvement initiatives for poorer families, and the preference for home ownership, these policies do not seek to capture and reinvest affordable housing financing into more affordable housing or dividends for shareholders. These policies instead, act as a measure to ensure households can afford rent or mortgage payments in the private sector.

2. Where Social Housing Sector Does Not Already Exist: In some jurisdictions, demand for housing is focused on the movement from informal, temporary and self-built houses to permanent, formal structures that can be commodified as part of a wider housing market (i.e. where homes may be resold at a value more than the land these homes occupy). This is the case in many developing countries. Where little formal housing exists, particularly at the bottom end of the market, the jurisdictions usually also have little to no affordable housing stock to borrow against (i.e. these affordable homes do not exist) or that has value to borrow against (e.g. they therefore do not have rental products, and therefore rental income streams). This is further compounded where there are high interest rates as the result of large scale borrowing by government (c. 12-16% in Rwanda). To form housing institutions, some go to the capital markets (i.e. in countries where economic outlook/return is positive, and currency is stable) and to international aid agencies and development banks (i.e. The World Bank). International Aid organisations also help promote institutions to enable more affordable financing options in jurisdictions where interest rates are high. Since 1982, the World Bank has taken an

approach to promoting housing market finance through facilitating the capital markets and self-sustaining mortgage institutions with capacity to making long-term mortgage loans to low-and moderate-income households.

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Part 2: Responses & Learning from the UK's process

The UK social housing sector has responded to decreased public funding and changes in macroeconomic policies and political priorities over time. The process has been:

1. **Pre-1919: Private money pays for affordable housing institutions**

   Problems of poor housing conditions, mostly in inner city areas, grew steadily as city populations increased during industrialisation.

   Housing associations (HAs) first appeared in the nineteenth century, where they were part of the emergence of various philanthropic and voluntary organisations. Early examples are the Guinness Trust, Peabody Trust and the Metropolitan Association for Improving the Dwellings of the Industrious Classes.

   Government intervened in housing minimally in the latter half of the nineteenth century through acts to improve or demolish housing unfit for habitation but did not actively build housing until after WWI.

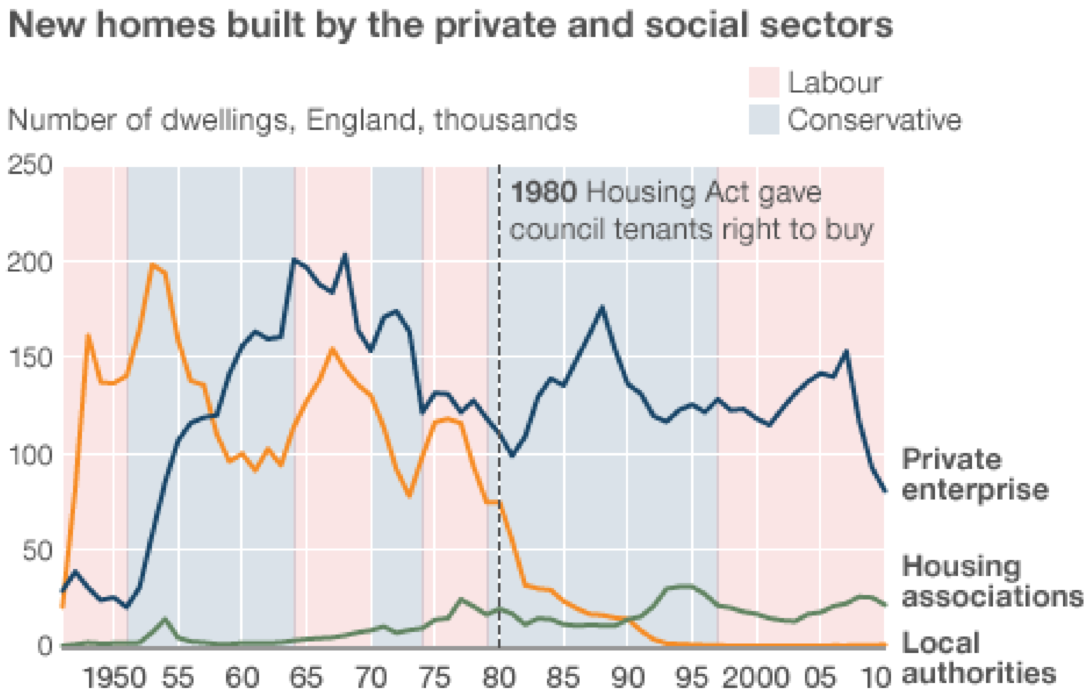
2. **Post-1919: Public money pays for affordable housing institutions**

   A programme of local authority council house building started after WWI following on from David Lloyd George's government's Addison Housing Act of 1919 (i.e. "Homes for Heroes" era). The Act promised government subsidies to help finance the construction of 500,000 houses within three years. But the rapid economic decline of the 1920s meant funding had to be cut, and only 213,000 homes were completed under the Act's provisions.

   Large scale demand for council housing continued into the post-WWII era as a result of severe housing shortage of c. 750k homes. In 1945, a Labour government was elected with supply-led housing policy central to their agenda. The Labour government utilised new technologies such as prefabricated housing, considered a temporary measure at the time. In the decade after 1945, 1.5 million homes had been completed by government.

   Following the post-war housing boom, the UK government (during Conservative and Labour administrations) continued to provide significant capital subsidies into local authority housing (new supply and investment) until the 1970's. Political difference was focused on the target need groups for new supply (i.e. lower and middle incomes, or just lowest incomes) and the type of supply being produced, including technologies, densities and placemaking characteristics. The last big push for council housebuilding was in 1964 under the Wilson Labour government and Minister of Housing Richard Crossman. By the 1970s, councils built increasingly fewer homes, concentrating instead on repairs to their now ageing housing stock.

Figure 2: 2012 Analysis of new housing development by three groups (via Ministry of Housing, Communities & Local Government)



Also, during the post-war period and into the 1970s, considerable investment was made through regeneration and slum clearance programmes. Slum clearance in the 1950–1970s, a policy originating in the 1930s, was one of the biggest and most ambitious state-led programmes, even measured by the scale of public policy initiatives in the post-war reconstruction era (e.g. establishing the NHS, the formation of British Railways, etc). Clearing the slum housing legacy of the Industrial Revolution changed society in a very direct way. The Ministry of Housing and Local Government data suggests the clearances that took place between 1955 and 1985 affected about 3.70 million people, with some 1.5 million properties demolished. This means that these clearances affected nearly 15 per cent of the extant population.

HAs were marginal players at least until 1974, when a subsidy regime was put in place enabling them to build rented housing to be let at fair rents (i.e. *the 1974 Housing Act)*. Throughout the 1980s the Government moved towards a regime of reduced direct government subsidies. 1979 is one key date for housing policy discourse, with the election of Margaret Thatcher's Conservative government and subsequent introduction of a home ownership policy agenda. in the 1980s, legislation for local authority renters to be given the 'Right to Buy' their local authority owned homes shifted the policy focus from government-driven support for rental to government-driven support for homeownership.

In the late 1980s and 1990s, funding from government for regeneration introduced in the Housing and Planning Act 1986 was partially contingent on a shift from local authority ownership to transfer of stock to Housing Associations and Arm's Length Management Organisations.

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3. **Post-1988: Institutions may secure private finance against their assets and rental income streams**

The Housing Act 1988, considered “year zero” for HAs today, introduced private finance to HAs or “mixed funding” which reduced HAs’ requirements and expectations on government grant and revenue streams. This led to the first housing borrowing and the creation of ‘club’ deals and brokers, such as The Housing Finance Corporation. These changes created a new relationship between government and providers of affordable housing.

Since the late 1980s and throughout the 1990s, grant rates from government have been falling year on year, compensated by an increase in private borrowing by Associations and the development of a cross-subsidy model, involving the development of open market, for sale properties to generate surpluses, to be reinvested in the provision of rented homes.. The post financial downturn in 2008/09 and revised political priorities has caused this trend to accelerate, and we have observed over the last eight years, the Government's capital commitment to building homes has fallen from £11.4billion in 2009 to £5.3billion in 2015 (equates to 0.7% to 0.2% of the total GDP).

Table 1: GDP spent on housing development in European countries

% of GDP spent on **housing development** by “General Government”			
Country	2009	2015	2017 (most recent)
UK	.7%	.2%	.2%
Austria	.3%	.2%	.2%
Italy	.3%	.2%	.2%
Ireland	.7%	.1%	.1%
Switzerland	.0%	.0%	.0%
France	.4%	.3%	.3%
Luxembourg	.3%	.2%	.2%
Germany	.3%	.1%	.1%
Poland	.6%	.3%	.3%
Europe Avg	.4%	.2%	.2%

Via: Eurostat (European Commission), 2019

Before the 2008 global financial crisis, HAs were largely funded by a combination of government grant and long-term bank loans. But with tighter capital requirements post financial crash, as well as Basle II and capital cover requirements, banks are becoming less willing to lend for long periods at fixed interest rates. Basel II is the second of Basel Accords, published in 2004. It intended to amend international banking standards to control how much capital banks were required to hold to guard against financial and operational risks. Note: Basel II wasn’t fully implemented enough before the crash to be effective. This iteration is now partially superseded by Basel III, which consider the outcomes of the crash.

As a result, Housing Associations have looked to the capital markets since the 2008 financial crisis. The capital markets have contributed to dramatic growth in bond issues by UK HAs to fund the provision of social housing. More than £7.3bn, for example, was raised via the debt capital markets between July 2017 and July 2018. This represents 10% of the total debt currently held by RPs, who make up 90% of the social housing debt in England.

A variety of bond transactions are seen, but the two main ones are:

- "own name" issues: by an HA or a member of its group to raise finance for that HA or its group (i.e. Clarion plc issues the bond to Clarion HA)
- "pooled funding" issues: by a funding vehicle that raises finance on an aggregated basis and on-lends it to a variety of HAs (i.e. investment funds)

There are other types of institutional investment, including pension and insurance funds. Due to their long-term rental income streams and social-driven platforms for operation, HAs are seen by investors as safe, secure and ethical investments with assured returns and a zero-default record.

In 2018, the Regulator of Social Housing reported a significant increase in financing activity among social housing providers. The sector raised more than £10bn (2017: £7.6bn, 2016: £5.2bn) in new debt facilities from banks and capital markets. At March 2018, the sector had more than £17bn in undrawn loan facilities and £6bn in cash.

4. Institutions look to long-term rental income streams as an asset value appreciation for private equity finance

The Housing and Regeneration Act 2008 made a big change to the status-quo when it first allowed For Profit Providers to enter the market and register as social and affordable housing providers regulated by the RSH. Instead of reinvesting surplus into existing and new stock, these organisations use surpluses from rents and sales to pay dividends to shareholders. The aim of the policy was to allow for these organisations to contribute to the gap between demand and supply of housing. Currently there are 46 for profit registered providers who currently own circa 2,500 homes. And recently (early 2018) it was announced Blackstone, the world's largest real estate private equity investor, would invest into the UK's affordable housing sector. Other For Profit Providers include, Legal and General, M&G, and Man Group.

Note 2: Blackstone in Spain
Since 2012, the US fund has acquired property in the country worth almost €20 billion and it is now the owner of several listed vehicles, as well as of some of the main asset managers in the country.

With that figure, which accounts for 20% of the €100 billion that Blackstone Real Estate has invested around the world, the firm is the country's largest private manager of real estate assets, including properties and portfolios of mortgages.

The debate is contentious, with one view arguing the institutional affordable housing has and should always be provided through charitable or non-profit organisations. While the counter argument claims the sector is in a state of crisis and if for profit are fully compliant with the regulating standards then their inclusion and significant investment should be a welcomed one.

The Housing and Regeneration Act 2008, also saw the creation of The Homes and Communities Agency (HCA), now called Homes England, as one of the successor bodies to the Housing Corporation, the existing investment and regulatory body for affordable housing in the UK. Homes England has shifted government investment beyond direct subsidy for affordable housing development and into market enabling interventions such as equity loans (“Help to Buy”), and loan guarantees for developers. It has also fostered relationships with existing delivery agents, such as housing associations, but also new entrants, including For- profit private sector organisations and a resurgence of local authorities building new homes. The English affordable housing market is now characterised by a range of demand and supply side interventions which vary depending upon the priorities of the current government. And a mixed economy of institutional ownership ranging from state owned provision, through housing associations to wholly privately-owned companies.

The Regulator’s role in ensuring the viability, efficacy and probity of organisations who receive government subsidy/ investment has remained constant throughout this time and this regulatory regime is credited with enabling the borrowing of over £70 billion in the affordable sector at favourable rates.

Part 3: Examples of institutional ownership and financialisation

Rwanda

Context & Drivers: Economically developing Country with little to know existing social housing sector, high bank interest rates against local currency as the result of large-scale government borrowing to boost GCP (c. 13 – 16%). Research from the IGC indicates that in Kigali alone (Rwanda’s capital and urban economic centre), housing stock will in effect need to double (from c. 350k homes to c. 700k homes) over 2017-2032 to meet growing housing need. Currently, housing is provided through the private sector and is self-built on parcels of available land, with very small numbers of free housing made available for some impoverished households.

Responses: Government policy & infrastructure funding to attract institutional investment. In building new housing developments, they are looking to the capital markets or NGOs/Development banks to borrow to build and sell affordable housing, or to build and rent affordably.

Case Study: The Green City Pilot Project is looking to finance capital costs for affordable housing and maintain a sustainable institutional cash flow model through a combined cross-subsidy and long term rental income and service charge development through capital investment from the German Development Bank and possible other investors, and grant for green and climate mitigation elements from the Green Climate Fund. The government has committed to provide basic infrastructure funding. The World Bank has started a housing finance project to provide low interest-rate housing finance over the next c. 5 years, which can be used by programmes like the GCP. The main challenge of the project is to provide homes at a cost that local people can afford, while also providing low-cost financing options to individuals despite high national interest rates.

Delivery Agents: Government, NGOs, Public Private Partnerships

France

Context & Drivers: Developed country with one of the highest house building statistics in Europe (In 2017 nearly half a million new homes were built) driven through government backed financial incentives – mostly centred around tax breaks.

Responses: Government policy has allowed 'HLM' organisations (HAs), which are specific actors entrusted by the state to fulfil a mission of general interest providing housing at moderated rents. The social housing sector in France accounts for about 17% of total housing stock.

Case Study: Rents are based on construction costs. Most of the funding for new construction comes from finance loans, where the main lender is through the public financial institution CDC which provides funds from the 'Livret A' accounts. This is a savings fund with regulated interest rate and not subject to tax. Every French household has the right to open a tax-free savings Account at their local bank. Their savings are pooled by the CDC, which pays a fee to the banks for collecting the funds and a defined interest rate.

However, France still has several challenges. By law, at least 20% of housing in every town across the country must be social housing, which has caused a number of 'ghost cities'. Additionally, as demand is unevenly spread, simply building more homes does not solve the problem, there needs to be greater consideration to where those homes are built and who for.

Delivery Agents: Quasi-Public Sector Housing Developers and Landlords

Vienna (Austria)

Context & Drivers: Vienna has kept housing affordable for its residents for the last century through the city owning much of the land and using municipal developments to keep renting costs low. Historically Austria has had a strong tradition of supply side housing subsidies founded upon a strong tradition of social renting carried over from the ‘Red Vienna’ period of the 1920’s (80% of the population today rents, with more than half of the population paying sub-market rent).

Responses: Austria has decentralised housing policies to municipalities allowing for flexibility and control over managing the housing market and maintaining affordability. A focus on supply-side subsidies has kept Austria’s expenditure on social housing by percentage of GDP lower than the UK and many other EU countries, with demand-side subsidies helping only the lowest income families. Additionally, eight out of ten flats built in the city today are financed by Vienna’s housing subsidy scheme.

Vienna’s city-owned development corporation allows for strategic ‘land pooling’ and quality-control of developments and is already an approach the Greater London Authority are considering for transport-oriented development.

Case Study: The city of Vienna is Austria’s largest homeowner with 220,000 rental apartments. The financing of social housing, both in the rental sector and in the subsidised owner-occupied and single-family housing sector, is based on contributions form national taxes and from the regional budget. The national tax revenues are distributed to the nine provinces based upon a complex financial agreement, with Vienna receiving €450m each year from central government for housing purposes giving it a €600m budget (about equal to that of London, despite a population c. eight times smaller).

The cornerstones of Vienna’s social housing are 220,000 municipal homes as well as a further 200,000 subsidised homes. Allocation guidelines that also grant those households on moderate incomes (as opposed to exclusively low-income families) access to this large and growing housing sector ensure an adequate social mix.

Delivery Agents: City Municipality, Wholly Owned Development Corporation

London (United Kingdom)

Context & Drivers: London has high housing costs and the Mayor has recognised that for young families and individuals on average incomes, housing is becoming increasingly unaffordable – with home ownership far out of reach for many. London is not building enough supply, particularly affordable housing supply, to meet demand.

Responses: The Greater London Authority and partners have introduced a suite of interventions in the Capital, either promoted centrally by policymakers or taken on by some of the delivery agents outlined below. Generally, responses are to deliver more affordable supply (the Mayor set out targets to deliver 50,000 homes per annum during his administration), but the Mayor is also concerned with giving tenants renting in the private sector more rights, including rent caps against rapid rental increases, which exacerbate affordability issues.

Case Study: In his campaign Manifesto, "A Manifesto for all Londoners", 2019 Mayor Sadiq Khan outlined that his top priority was to "tackle the housing crisis, building thousands more homes for Londoners each year, setting an ambitious target of 50 per cent of new homes being genuinely affordable, and getting a better deal for renters". The Greater London Authority have since introduced and advocated for a series of policy measures to improve housing affordability and access in London. These include measures that address land availability for new development (for example on public sector land, such as Transport for London), rental affordability in the regulated social and non-regulated private rental sectors (including through a recent push for legislative powers to enact rent control measures) and to promote the use of new development agents to expand development capacity (such as Local Authority wholly-owned development companies). Some of the secondary goals of the Mayor's policies include fostering new technologies and innovation in the delivery of housing and achieving housing density while also fostering inclusive communities.

Delivery Agents: Housing Associations and Subsidiaries, Local Authorities, Wholly Owned Local Authority Development Companies, For-Profit Affordable Housing Providers