

Section 1 Contemporary issues

Chapter 3

Private finance for affordable housing investment: from debt to equity

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The last few years have seen a rapid growth in the deployment of equity investment into affordable housing in England. In contrast to the established sources of finance from debt or bond investors who provide funds for new development on a secured basis, equity investors provide and retain an equity stake in the new homes. Equity investment in affordable housing is potentially attractive to pension and insurance funds. This chapter explores the issues around the changing nature of private finance and the prospects for a significant boost to the sector in the form of equity investment. It aims to explain how different types and different sources of capital can be best used in delivering new affordable housing.

The needs of pension and insurance funds

There have been many attempts to define the basis and terms on which we might envisage investment at scale from pension and insurance funds in affordable housing. These have ranged from a focus on the stable, secure, low-risk, asset-backed nature of the investment, through to pension funds having some form of 'responsibility' to invest in affordable housing in their local areas. After all, for pension funds the fundamentals should all align: the funds exist for the long-term, so do the homes; the funds have millions of pensioners (some of whom might also want/need affordable homes) and therefore the money to invest; they are seeking inflation-hedged investments of a low-risk nature to match off against the inflation-linked liabilities in many defined-benefit pension schemes and, by investing in affordable housing, they would undoubtedly be contributing to the social good.

It feels like we have been talking about leveraging in pension-fund investment for well over a decade. And we are still talking about it now: witness the recent push from government to get local authority pension funds to invest in 'levelling up' in their local areas.¹ Leaving aside the challenges associated with that initiative, is any progress being made?

There has been talk of a 'wall of money' waiting to find the right assets for long-term, low-risk investment. We hear more and more about environment, social and governance (ESG) investing² – and how institutional investors worldwide are

seeking this type of investment to prove their credentials in terms of social responsibility. One might be forgiven for thinking that we are still talking about it rather than doing it – and in many ways there is so much further still to go.

However, it is undoubtedly the case that investors have begun to make their moves, and there are several ways in which we can judge that equity investment from pension and insurance funds is rapidly becoming not only the 'next big thing' but possibly even the major basis through which future generations of new affordable homes will be financed. Moreover, despite initial scepticism from housing associations and local authorities, there are definite signs that the 'traditional' social housing sector is responding positively to the opportunities that this scale of funding potentially brings.

A brief history of housing association private finance

Until the mid-1980s, all social housing was supported by public or charitable funding. Delivery was almost exclusively through local authority direct provision of council housing. Many small housing associations (HAs) had also been created, in most cases to fill gaps unfilled by council housing (for example, specialist provision for specific groups of people).

Housing legislation during the 1980s introduced private finance at scale into the housing association sector for the first time, where HAs would borrow alongside capital grant provided by central government. Banks and building societies lent on favourable rates (relatively low margins) over long terms (typically 25 years) to HAs, building up the best part of £55 billion of investment in the period up to the global financial crisis (GFC) in 2008/09. The funding model fitted the operating model very well – net rental income covers debt costs over the long term, driven by indexed rent increases of at least RPI (now CPI).

The recapitalisation of high street banks post-GFC meant that access to cheap, long-term debt was restricted. In some cases, banks were 'underwater' (losing money) on much of their earlier lending and consequently wished to renegotiate loan portfolios with associations. As a consequence, HAs made much greater use of the capital markets for long-term funding. This has delivered around

£25 billion of funding to date, commencing with the large players (Places for People, L&Q) but now extending right across the sector to relatively small associations. The bond issuances are well-suited to the high-demand, long-term inflation-linked and stable nature of affordable housing. There has been a full range of tenors (the length of time over which bonds are issued) ranging from ten years to 40+ years, with sizes starting as little as £50 million up to £350 million and even larger. The market has matured significantly and the rates of interest that are paid on bonds are now extremely competitive. There are three principal reasons for this: first, investors are looking for the strong ESG credentials of the HA, and will reduce their return needs to reflect ESG; second, the HA sector has a high degree of 'income stability' (i.e. it is low risk) and third, there is a huge weight of capital wanting to invest which also helps drive rates down.

This is all relevant as bond issues introduced new types of investors to HAs, including many UK and overseas institutions and pension funds. Many have become familiar and comfortable with the features, risks and rewards of the sector, and the strong regulatory backdrop which provides comforts for investors and others. The Regulator of Social Housing (RSH) has not seen any association ever in default and has, to date, always found a suitable purchaser or merger option for those small number of HAs that have got into trouble. The same applies to equivalent regulators across the UK.

The regulated status, as well as the steady income stream of general needs, affordable housing rents, have generated a huge amount of interest from investors, which continues to build momentum. Particularly during periods of economic uncertainty and volatility, capital has flowed consistently into associations as investors have sought quality and safety. There are plenty of examples in recent months that highlight this peak in demand, these include Clarion's £50 million 2048 bond in 2021 which priced at 0.88 per cent over gilts and LiveWest's benchmark primary issue of £250 million 2056s, which priced at 0.90 per cent over gilts and was substantially oversubscribed.

We have reached the point where private finance dominates the funding of affordable housing, being much more significant than grant. While the position is

different outside England, Commentary Chapter 4 points to an RSH estimate that grant covers only six per cent of the capital costs of all new affordable housing, while a recent National Audit Office report assesses grant as covering just 24 per cent of costs for grant-assisted schemes, with 46 per cent covered by debt.

Wider financing options and equity funding

The solid track record of bond and debt funding has naturally led investors and fund managers to consider their options for deployment of wider pools of capital. While debt funding is a solid investment, it is not generally index-linked and so there is work to do for investors to create the right basis to match index-linked pension liabilities, by converting fixed streams of income received from debt lent to the sector, into index-linked payments to pensioners.

In the last decade, investors have therefore also begun to focus on equity funding, making direct investment in affordable housing and unlocking the potential for genuinely inflation-hedged investment at scale. Investors initially focused primarily on leased property in which the covenant strengths of local authorities and HAs were the key to low-cost funding. In this type of funding, the investor passes all the risk on (for example) rent collection to the lessee, so that even if there is no rent collected, the lease payment is still payable – in this case, the financial strength of the LA or HA keeps the cost of funds low. The first long-term reversionary-lease deals, where the investor has a right to possession at a future date, were undertaken with HAs in the early 2010s and a small number of such deals have also been struck with local authorities.

However, partly due to reticence on the part of HAs and local authorities (where straightforward debt represents a cheap, familiar and less complex source of funding), and partly also through poor understanding of the products on offer, the amount of capital deployed through leases in the mainstream affordable sector has so far been limited. The RSH has also had cause to make compliance interventions relating to lease structures – most notably with Cosmopolitan a decade ago but more recently, and continuing, with very small providers in the specialist supported housing sector.

Nonetheless, in response to the lack of demand from counterparties and reflecting what were until recently historically low gilt yields, lease terms have improved and are now becoming more balanced in risk-sharing – with the funds taking a greater risk share – leading to a wider diversification of offers being made on all sorts of different terms. These developments have produced results, with more lease deals being completed: most recently, for example, with the London Boroughs of Bromley and Barking & Dagenham.³ Yields remain competitive in the context of interest rates, gilts and other key global factors and despite recent adverse moves in the market.

The emergence of for-profit providers

The limited appetite for lease structures may have persuaded a number of investors and funds to set up their own for-profit registered provider (FPRP) structures and to directly own, fund and operate affordable housing – taking on the associated income and operating risks. And from 2018 onwards, FRPPs have emerged as the main engine for growth in equity investment.

Legal and General Affordable Homes, MAN Group's Habitare and M&G's RP exemplify the shift from being a lender to becoming an owner-operator. ReSi housing, Heylo and Sage Housing are all examples of leading new equity entrants now holding properties in FPRP entities. Other new equity entrants (such as CBRE IM) have not set up their own FPRP but work through lease structures with HA partners. There are currently 69 FPRPs registered with the RSH and a large number in the registration pipeline.

At the same time, bond issuances continue, and banks/building societies continue to lend actively to the HA sector. The availability of private investment across a range of these new, equity-related forms is however beginning to make a very significant contribution with an estimated £8 billion of equity in total now deployed over the last ten years, most of which occurred in the last 3-4 years.

The affordable housing sector has tended to use the catch-all phrase 'equity investment' to describe the new entrant capital that is available to deploy through leases and FPRPs. While this is a helpful term, it masks the wide range of types of

equity and funds seeking looking to invest in affordable housing and how they differ from each other. As more funds deploy and leading early-mover FPFs become more established, acquisitions and deal structures are evolving to produce a meaningful and plentiful supply of equity which is set to make a lasting impact on the sector.

What is in it for investors?

Even in a volatile economic world of higher inflation, higher interest rates and generally higher cost of capital, the relative status of 'affordable housing' as an investment class has not changed. These are the key motivators driving the appetite for this kind of investment:

- *Structural imbalance – persistent under-supply of homes – long-term government support.* Investors seek long-term investment models where there is a market imbalance to address over an extended period. Affordable housing is under-supplied, and the majority of income supporting its delivery (i.e. rents) is paid for from housing benefit or universal credit (i.e. the government). This is further emphasised by the underlying demographics – an ageing population, with new offers in older persons' housing, care and support, extra care, etc. being developed all the time.
- *Long-term, stable cash flows with indexation – provide an inflation hedge, leading to lower cost of capital.* Taken over a long timescale, liability matches to pension payouts; really secure, index-linked investments are rare in the market and affordable housing is one, therefore attracting the lowest costs of funds.
- *Exposure to residential real-estate market cycles through house-price inflation in shared ownership.* Another key factor is that the regulated affordable housing sector tends to come not only with long-term, secure rental income, but also increasingly offers shared ownership – which gives an even more secure RPI+ income stream from rents, with increasing comfort that staircasing proceeds can be reinvested quickly to maintain returns.
- *There is little correlation to other typical real-estate asset classes with rented tenures.* It is difficult to imagine anything less correlated than affordable housing compared to, say, retail and commercial investments. Relatively speaking, the housing sector will always be an attractive investment and changes brought on

by the Covid pandemic may well have emphasised the volatility of investment in other asset classes.

- *Robust ESG credentials.* HAs have positive attitudes towards addressing climate change and sustainability, with many already developing their longer-term net zero strategies and targeting step-change increases in energy efficiency. The social impact of affordable housing providers is beyond doubt. But the governance point is also critical – stable, independent boards of governance, clear accountability for delivery, backed by a strong regulatory framework. All the ESG factors are ‘ticked’.

As none of these drivers are likely to change significantly soon, it is possible to say with some confidence that the appetite for equity investment in affordable housing will not diminish: quite the opposite, as more investment drives more returns, and more investors get interested and then get more comfortable with the sector. Appetite is likely to increase.

In fact, the ESG angle could be decisive in shaping investment behaviour going forward. We have already seen over 100 HAs sign-up to a voluntary *Sustainability Reporting Standard* on debt⁴ and it is almost certain that the new market norm will be ESG-compliance, meaning that those that are not reporting on ESG might face higher costs of funds. But we are also seeing investors flexing their ESG muscles to influence investees – witness the recent action from groups of investors to put pressure on oil companies to take their climate-change strategies seriously.

Regulated affordable housing in England is well-placed to take up this investment. In turn, these factors are likely to drive a wider range of types of deal and more diversity in the kind of partnerships that are developed between investors, FPRPs and the ‘traditional’ HA and LA sectors.

Some of the developments around partnerships are explored in more detail below. Given the prevailing economic and inflationary context, and pressures on the existing asset base through building safety and preparing for net zero, it is possible that equity investment will, over time, become the dominant source of

capital for new affordable housing development. Certainly, that is Legal & General’s assessment⁵ – and whilst we are definitely still in the early stages, there are plentiful reasons for thinking that this is the general, long-term trend.

Prospects in Scotland, Wales and Northern Ireland

The focus of new entrant investment has to date been in England, with a small number of deals in Scotland. Previous proposals for Wales have not yet come to fruition. The concentration on England has been driven by the scale of need and demand, and therefore the scale of the addressable market and the opportunity to deploy significant amounts of capital. But another reason might be the availability of opportunities to vary the business model and therefore the basis for investment. For example, the legislation allowing ‘for-profit’ providers has not been replicated in Wales or Scotland and no new RSLs have been registered in Scotland for more than ten years.

Therefore, the focus of the limited number of deals in Scotland has been on sub-market, affordable private renting, as opposed to investment in new forms of social housing. The promotion of ‘mid-market’ rents has been of particular interest to investors and the Scottish Government has generally been willing to support new forms of private capital, especially with the operation of guarantees. There is a history of supporting investment in the PRS via the Private Rented Sector Housing Guarantee and a recent consultation (Autumn 2022) on a Rental Income Guarantee Scheme.

In Wales, the government has tended to work closely with HAs and local authorities to lever in private finance via the existing landlord businesses, rather than to seek new approaches to lever in private finance directly. For Northern Ireland, the unique circumstances in which the Housing Executive operates as both a policy-directing, strategic body and as a landlord almost certainly makes the policy environment rather too complex and locally specific for investors to embrace readily. There may also be a question of scale of opportunity. This is not to say that investors are not interested, rather that it remains to be seen whether specific approaches in Scotland, Wales and Northern Ireland can bear fruit in bringing forward more affordable rented homes at scale.

Fund types

Whilst 'long income' and liability matching underpin investments in affordable housing, it is worth highlighting the different fund types and different investor types who seek different risk and return profiles – and this can also drive value for the sector. All types of fund are active in this market and some examples are given in the box.

Types of funds

- Long-income/ retirement and annuity funds – seeking long-dated, index-linked stabilised assets with as little interruption to returns as possible.
- Core/ Core plus funds – seeking investment over a medium term with the option kept open to hold for a long time or sell onto a long-income fund; this type of fund will be comfortable acquiring stabilised assets and in forward-funding new development (for example, section 106 acquisitions or development schemes).
- Value-add/ Opportunistic funds – as the name suggests, seeking additional returns over a generally short-to-medium-term period, seeking an exit by selling to a long-income or core fund; this type of fund will target forward-funding and new development, seeking higher returns from what is seen as a higher-risk investment.

Often the shorter the term, the more likely the fund will look to take on debt to help leverage the equity investment – in effect to make the equity work harder to drive increased returns. Investors can supplement equity funds by taking on additional debt – this gives the opportunity to acquire more properties for a given amount of equity. For value-add funds, we see leverage of up to 70 per cent, for long-income funds, it is equity only.

It is always the case that the higher the risk, the higher the required return. All types of capital seeking all levels of return have their place in this market and there is nothing inherently incompatible between value-add funds engaging in forward-funding of development at risk, then exiting to a long-income fund when everything is built, fully rented and hence stabilised. We will see this cycle play out in the next few years as these funds reach their set maturity dates.

But it is also critical to recognise that the ultimate investors (i.e. the sources of capital being invested into funds which are then invested in affordable housing and FPRPs) all tend to go back to pension funds and insurance funds. Pension-fund trustees would be expected to balance risk and return across their enormous portfolios – and that is precisely what we find: local authority pension funds, for example, will invest some money into value-add funds and some into long-income funds.

How do we expect to see the market grow?

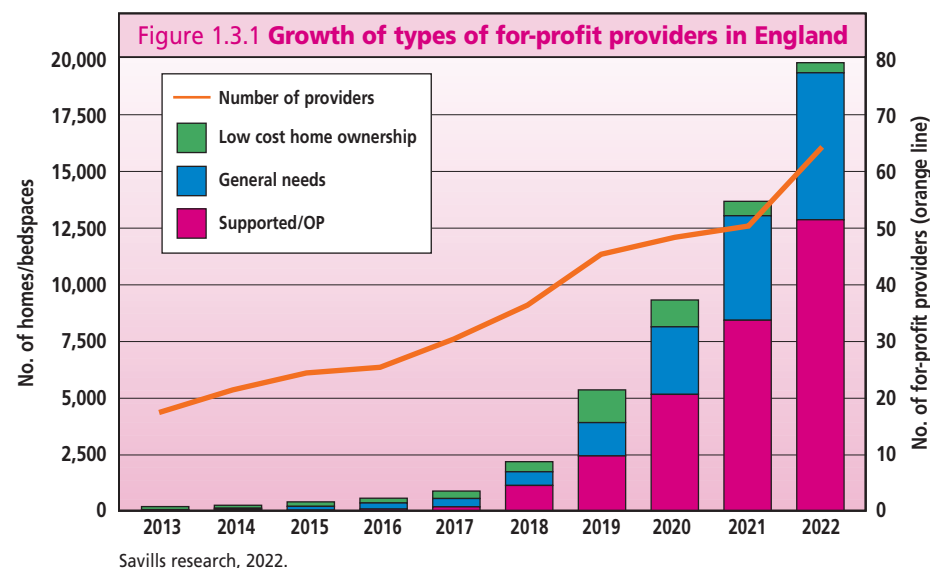
Research undertaken by Savills in 2022 captured a 'point in time' in the evolution of the market and will be followed-up in 2023. Here are some key findings.

Growth in FPRPs.

There were 69 FPRPs at the end of 2022, of four broad types:

- *Developer-led*: 29, including large multi-national, national/multi-regional, local-SME FPRPs, split between those set up early to allow acquisition of affordable homes on site and those set up recently for delivery of a specific pipeline of developments – all ranging in size but focused on specific areas for growth.
- *Local authority and existing HA-owned*: 4, but numbers could be set to grow as existing larger HAs may seek to rationalise stock balance sheets and raise capital in partnership with investors and funds.
- *Specialist*: 10, a range of specialist providers including some care/support and some lease-based for temporary accommodation and other specialist accommodation.
- *Investor led*: 26, in practice, this covers a wide range, including ones that have grown in the last 3-4 years (Resi, Heylo, Sage, Legal & General Affordable Homes – which make up just less than half this total as some of these investors have multiple FPRP entities) and those that have been established but are yet to achieve scale (for example, M&G SO, Man Group's Habitare, Octopus's Newmarch, HSPG's Park Properties); there is a range of other funds with vehicles in place to take advantage of specific local opportunities (for example Williams Pears' MTD Housing, Matter Real Estate's shareholdings within St Arthur Homes and Auxesia Homes).

It is this small group of investor-led FPRPS that are driving real growth, in particular since 2018 (see Figure 1.3.1), with nearly 20,000 homes financed by about £8 billion of investment deployed or committed to date.



Looking ahead

Reviewing plans for investment, we can expect to see growth to continue apace, with what Savills considers might be as much as £27 billion invested in around 140,000 homes by 2027 (Table 1.3.1). Likely key developments include these:

- Shared-ownership supply is expected to average 21,000 homes per year. Of FPRP stock in 2017, 20 per cent was low-cost homeownership; it rose to 66 per cent in 2022, and is forecast to be 63 per cent in 2027 as the grant focus may well shift back to affordable renting.
- Large providers (more than 500 homes) own 91 per cent of the existing FPRP stock but those same providers will only own 76 per cent of stock in 2027 as newer FPRPs catch up.
- Three FPRPs with no completed stock as of 2022 have plans to exceed 1,000 homes in the next five years.

Table 1.3.1 Numbers and projected numbers of for-profit providers in England

	2017	2021	2022	2027		
				Current FPRPs	Additional FPRPs	Total
No. of FPRPs	31	51	64	64	c.25	c.90
No. of homes	873	13,671	19,600	111,400	c.30,000	c.141,000
Capital (£billion)	0.2	2.4	3.7	21.2	5.7	26.8

Source: Savills research, 2022.

Put another way, if new investors and FPRPs are accounting for upwards of 25,000 new homes a year by 2027, that could represent nearly half of all affordable homes delivery by that time, raising substantially the output of homes for shared ownership. There might even be reasons for believing that this is an underestimate given the growing pressures on the traditional HA and LA sectors.

What might interrupt this progress?

Investment is driven by policy and financial stability as well as the under-supply of affordable homes. There have been some strong headwinds influencing progress since early 2022:

- *Inflation and economic volatility:* the normal low-inflation environment has been interrupted and this affects affordable housing specifically in the delivery of services to residents and, ultimately for investors, also flows through into the costs of funds. Whilst the relative position is unchanged vis-à-vis other investments, equity returns across the board have risen.
- *Interest rates:* those funds reliant on some measure of debt to make their investments work are likely to find themselves less competitive than they were until rates began to rise last year, which in turn is likely to have interrupted progress until debt terms can be realigned.

- *Policy instability*: changes in the Affordable Homes Programme 2021 caused some uncertainties (for example, shared-ownership schemes covering repairs costs for the first ten years, rent-to-shared-ownership options, minimum staircasing of one per cent). Investors will always point to a need to set quality standards and stick to them, but uncertainty has been caused by the cap on rent increases of seven per cent in England, together with the NHF-led voluntary cap on shared ownership rent increases, leading to below-inflation increases in income. Whilst seven per cent will be challenging for many social housing residents, net income does decrease in real terms, with the prospect of continued high inflation into the Autumn of 2023 potentially affecting rent increases for 2024 as well.

Funders and investors would like to see government and the regulator provide stability in rents policy, set out over the long term, so that investors and fund managers can plan over a timescale, take a view on current levels of volatility and thereby keep the cost of capital as low as possible.

Not separate sectors: what partnership offers

The FPRP sector is often seen as something completely distinct and separate from the 'traditional' not-for-profit sector. In many ways, the early days of new entrant investment may well have caught some HAs by surprise as a new source of competition came into the market. Certainly, the sector tended towards expressions of degrees of scepticism, particularly around what might have been perceptions of the motivations of investors, and whether affordable housing could meet what were (at that time and misleadingly) seen as higher return requirements.

As this chapter argues, however, times have changed, and whilst learning is still going on, there are very good reasons to expect that the social sector will embrace new forms of partnership with equity investors in the next few years. Some of the drivers have already been discussed: pressure on HA finances combined with a need to focus on the existing stock, the sheer volume of capital seeking deployment, the strong ESG characteristics of the sector. This latter is critical – every single one of the main movers from the investor community have partnered with traditional HAs for housing and property management – initially for management agreements but all part of the 'getting to know each other' dynamic.

For housing associations, equity investment offers the following:

- *Access to investment capital*: whilst lending from banks/building societies and bond issues will continue, the huge volume of capital available for equity investment is a key potential future source for HAs, who are in a good position to make a strong offer to investors (for example on ESG, and their ability to provide quality services).
- *Continue to grow operational platform*: by accessing capital from new sources, HAs may not necessarily be the owners of new build properties, but they will be able to utilise their established approaches to service delivery to continue to grow their service platform (i.e. the delivery of management and repairs services).
- *Maintain development expertise and output*: again, by accessing capital from new sources, HAs will be able to maintain and potentially grow their development teams to manage and deliver new developments, albeit financed by investors.
- *Cross-pollination of knowledge from other sectors, and other sources of investment*: as HAs and LAs learn more about investors and the new types of funding, so investors find out more about operating social and affordable housing, leading to greater opportunities for partnership.
- *Financial market-tested risk and governance processes that have been applied to social housing for decades*: the importance of the regulatory and track record of HAs in utilising private finance for 40+ years cannot be under-estimated – not one £ of funding ever in default and a strong record of independent and quality governance at board level.
- *Potential access to new opportunities from FPRPs active across multiple living sectors*: some HAs have diversified into delivering other tenure types, including for example market renting and student accommodation; many investors also have these additional 'living' platforms.

For equity investors, housing associations and the existing sector offer the following:

- *Rapid access to properties to accelerate deployment and growth*: one of the key targets for investors and fund managers is scale, i.e. actual deployment of capital; working in partnership with HAs can offer such scale.

- *Access to experienced developers and operators of social housing:* the established track record of the HA sector in delivering developments, and in managing and maintaining properties once built, are key strengths as investors can work with established providers rather than set up their own platforms from scratch.
- *Involvement of non-profit HAs (or LAs) adds credibility to development schemes:* most investors and fund managers are extremely concerned about reputation, particularly as they are investing pension fund monies on behalf of millions of ordinary people; the involvement of HAs and LAs is definitely a reputation-enhancer for investors. Additionally, as noted above, there is a really strong ESG angle to working with HAs and LAs.

Types of partnership

What types of partnerships are emerging? Here are six examples which give a flavour of how the market is evolving and how the non-profit and for-profit sectors are beginning to collaborate. Some are well established, some are just getting going, but all are likely to play their part going forward:

- *Long leases:* In many ways, this is where equity investors came in, and where long-income investment feels most comfortable, drawing upon the covenant strength of a larger HA or local authority; the model accesses freehold or long-leasehold properties, investors lease to the LA/HA over a long period, index-linked generally at CPI (although returns are even lower for CPI+ leases), with a reversion to the LA/HA for £1 at the end of the lease – a type of index-linked finance. This may well continue to be a small minority of completed deals, but they are likely to have a place, perhaps for local authorities with their wider placemaking roles, where authorities gradually get more comfortable with index-linked funding.
- *Sale of HA pipeline to a FPRP/investor:* An HA allocates and sells some of its development pipeline to an investor, maintains the development management role to deliver the new homes, and then manages the properties when built. The investor finances the developments (what is known as ‘forward funding’ i.e. funding in advance of the properties becoming income-producing), creating more headroom for the HA to invest in other elements of their business plan. There are several examples of such deals, most recently Legal & General with Metropolitan Thames Valley.⁶
- *Sale of HA development pipeline into a joint venture with FPRP or investor:* An HA allocates and sells some of its development pipeline into a joint venture (JV) with an investor with a FPRP, with different models of JV structure but essentially all focused on joint ownership of the provider that owns the stock when built. The development management role and future management and maintenance roles are retained by the HA.

The key example here is AXA and Hyde entering into a jointly owned 50:50 FPRP called Halesworth Housing.⁷ Whilst there is just this one currently, it might be expected that FPRPs jointly owned by HAs and investors will become more commonly used, as HAs are then able to influence the direction of growth of the FPRP. Whilst Halesworth is a 50:50 arrangement, many investors are likely to want to seek majority control of a JV organisation, particularly as the mandates (i.e. what they are allowed to invest into and what they are not) might stipulate that the fund/investor has control over the future of the JV organisation.

Examples of a full range of JV structures are likely to emerge soon, and all would represent additional capital invested in affordable housing. In no sense is this a ‘takeover’ of traditional HAs by new investors, rather both sides working together to find new ways to achieve each other’s objectives.
- *Sale of stabilised assets into a FPRP/Joint Venture structure:* An HA sells a portfolio of established income-producing stock to a FPRP/investor, raising capital for reinvestment into other priorities and continuing to manage the stock. To date, the focus has typically been on shared-ownership properties as they are seen as particularly low-risk by investors, and the post-sale management arrangements remain relatively straightforward as costs are low and do not cover repairs. Whilst Hyde are also the key exemplar for this approach, with M&G the investor, it might be expected that more of the larger shared-ownership stockholders will consider similar options. There are upwards of 200,000 shared-ownership properties within the HA and FPRP sectors currently: tens of £billions of value that could potentially be released from HA balance sheets for reinvestment.
- *Investment into new development via a framework:* Not all partnerships need to be focused on new structures: there are examples of investors and funds simply financing development pipelines through a framework or other form of ‘right of first refusal’ (ROFR) agreement. This could be partnerships between investors and existing ‘traditional’ HAs or for newly created FPRPs seeking to grow, particularly those led by developers where there is a pipeline of sites and the

opportunity to provide affordable housing supply, but where the developer is seeking new sources of funding to ensure the developments can go ahead.

A small number of such partnerships are at an early stage of development (in early 2023), with the potential for this arrangement to grow. The key benefit for the FPRP/developer is to secure funding, the benefit to the investor is to deploy capital, but the 'ROFR' approach does not tie the parties into a fixed JV structure, thereby leaving more flexibility for the parties to seek funding or investment elsewhere as appropriate.

- *Management agreements for new FPRP stock:* This is by far the most common approach to partnership working to date. FPRPs and investors seek partnerships with established HAs to bring their expertise to help deliver against the regulator's standards and to offer experience and a track record as the FPRP grows. Sage and Heylo use one HA, Legal & General Affordable Homes use a panel of 13 HAs. Management agreements are not generally long, usually for no more than ten years and frequently shorter; generally, there is a split of risks and rewards between the parties – for example on arrears, void periods, lettings and repair costs. This type of shorter-term arrangement works especially well for newly created FPRPs where there is not (yet) the capacity to manage and maintain properties. They can draw on the expertise and track record of the HA sector, which offers reputational advantage in the context of the RSH (i.e. an investor partners with an existing HA to add to their social investment credentials).

It works well for a HA to grow their management services at a time when they may be constrained in financing new developments and section 106 acquisitions. It is, put simply, an ideal way to 'get to know each other' and examples like this can be expected to grow and diversify in the next few years as the appetite for further collaboration grows.

Conclusions

There is massive interest from investors worldwide in affordable housing in the UK, and specifically in England. There is also a growing interest from housing associations for alternative funding solutions to support investment and growth.

There is a mix of activity and a range of models and there is an emerging market for all types of partnerships. The key market drivers are clear, and despite the challenges of inflation, interest rates and general economic volatility, they are unlikely to fundamentally change:

- New equity investors focus on the acquisition of section 106 schemes and grant-funded development schemes – with the likes of Legal & General Affordable Homes and Sage having led the way.
- New equity investors finance housing association development pipelines as HAs 'retrench' into asset management on their existing stock (dealing with fire and building safety, net zero and energy efficiency).
- New equity investors acquire stabilised housing association assets with management maintained by the HA, releasing capital for HA reinvestment – there is a large pool of buyers with FPRPs capable of acquiring at scale.

Just as occurred with the introduction of private finance in the 1980s, leading to a rapid growth in debt funding over a sustained 25-year period, the new age of equity investment has arrived and has really begun to 'kick in' from the late 2010s/early 2020s onwards. Far from seeing the growth of equity investment as somehow a separate sector, it is far more likely that such investors and the established sector will become important partners in addressing the supply and delivery of affordable housing, for decades to come.

Notes and references

- 1 See www.lgcplus.com/investment/gove-announces-plan-for-16bn-lgps-levelling-up-investment-31-01-2022/
- 2 For a brief explanation of ESG see www.investopedia.com/terms/e/environmental-social-and-governance-esg-criteria.asp
- 3 For details of the schemes, see www.pensioncorporation.com/news-insights/press-releases/2021/pic-invests-p67-million-in-innovative-bromley-affordable-housing; www.railpen.com/news/2022/trocoll-house/
- 4 See <https://sustainabilityforhousing.org.uk/>
- 5 See Legal & General and BPF (2022) *Delivering a step change in affordable housing supply*. London: Legal & General.
- 6 See www.mtvh.co.uk/news/mtvh-and-lg-affordable-homes-form-joint-venture-partnership-to-deliver-2500-new-affordable-homes/
- 7 See www.socialhousing.co.uk/news/hyde-set-to-hatch-more-for-profit-rps-79270