SOCIAL HOUSING OUTLOOK

BUILDING IRELAND'S FUTURE

With a new Government social housing strategy in place, the scene is set for a new collaborative approach, involving a range of different stakeholders, that will tackle Ireland's housing crisis.

With over 32,000 social houses currently under management, the social housing sector in Ireland expects to deliver an additional 5,500 units over the next three years and up to 15,000 of the 2021 target of 47,000 set out in the Government's *Action Plan for Housing and Homelessness,* according to Donal McManus, CEO of the Irish Council for Social Housing (ICSH).

"This year it's estimated that the sector will have up to 2,500 units sanctioned, which is a big increase on 2015 but, from next year onwards, we can expect to see an even bigger increase as some of the larger bodies ramp up their operations," he says.

The ICSH currently represents over 270 housing associations of various sizes, accounting for around 90% of the social housing stock in Ireland, and it has welcomed the recent publication of the Government's *Action Plan for Housing & Homelessness: Rebuilding Ireland.*

"We now have a very important *Action Plan for Housing and Homelessness* in place and it gives the sector something to focus on and, from the point of view of the banks, it provides clarity as it puts a more sustainable long-term financial framework in place," he says.

He adds that two of the key issues that will dominate the agenda for the duration of the *Action Plan* will be finance and capacity.

"The big themes for the sector will be capacity and the off-balance sheet funding that will be required to deliver these targets," he says.

"Some of this will involve the sector itself

Donal McManus
CEO, Irish Council for Social Housing (ICSH)

further enhancing capacity. However, increased capacity has to be enabled by other stakeholders in the public sector by having a pipeline of ready to go sites or properties, as well Government policies that support associations and their ability to grow their balance sheets.

"The Government's *Action Plan* sets out what is to be spent – bearing in mind EU fiscal constraints on its spending ability. While the Housing Finance Agency will still

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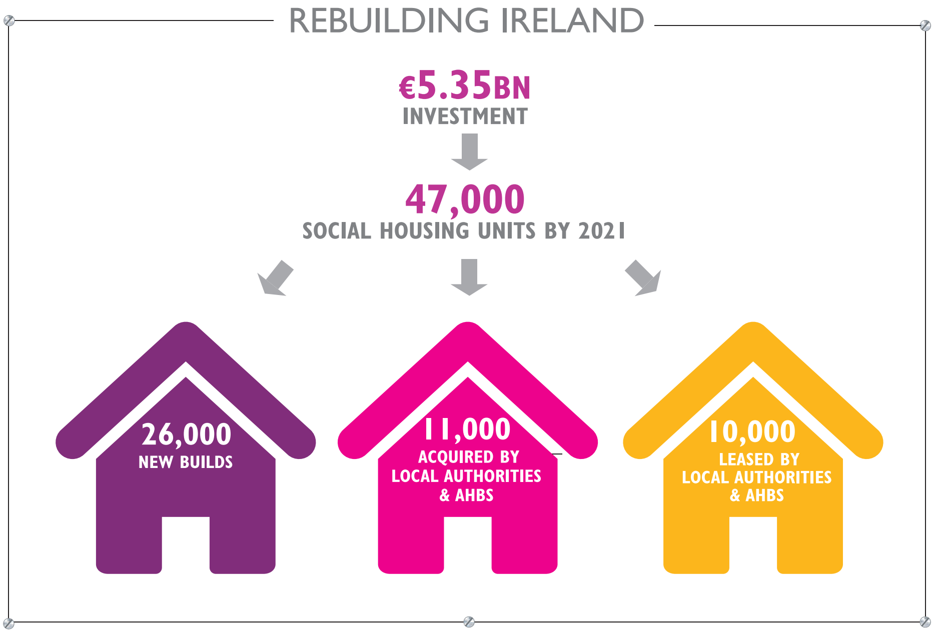
play a significant role, other mechanisms outlined in the plan have shifted the emphasis from capital expenditure towards revenue spending, including a strong focus on off-balance sheet state financing – whether it's from the main banks, other financial bodies or private equity or through various financial vehicles which the sector has been working on.

"We believe this is good as it introduces additional sources of much needed capital funding for an expanded programme. As the sector focuses on long-term planning, however, we need financial partners who >>



Source: Action Plan for Housing & Homelessness: Rebuilding Ireland can offer sustainable finance over the long-term," he adds.

To ensure that this new mixed-funding ecosystem is optimised, the ICSH would also like to see the various stakeholders work to a more streamlined, efficient and timely model of co-operation.

"The sector essentially has two different processes – one that involves State funding and one that involves non-State funding. When it comes to the latter, the decision-

"Many AHBs have also been strengthening their capacity while at the same time embracing the regulatory regime."

making process tends to require more immediate decisions and there needs to be a consistency in approach between the two. This is a partnership and we need to make sure that if we are taking on more risk to deliver more homes, things like site assembly and delivery by local authorities will be crucial," says Donal.

The emerging mixed-funding ecosystem is also leading some AHBs to explore a range of funding options as well as complementary services like affordable renting for people who would not be entitled to social housing but are being squeezed out of the private rental market, he says.

"Some bodies have put a lot of work into looking at affordable rental because it's part of their ethos to house people who can't afford to house themselves. It would also help take some pressure off the private rental market.

"The other interesting thing happening is that a number of bodies are looking at the potential of special purpose vehicles (SPVs) as a way of introducing additional finance into the sector and a sector-led financial vehicle has been included Government's *Action Plan,"* he says.

In preparation for the anticipated level of activity over the coming years, as well as to meet the appropriate regulatory standards that are required by potential investors and debt providers, he points out that many AHBs have also been strengthening their capacity while at the same time embracing the regulatory regime.

"Most housing bodies have increased their capacity and they have boosted their expertise in areas like staffing and the make-up of their boards. In terms of staffing, it's largely been focused on financial expertise and development while people with finance and legal expertise have been appointed to boards," he says.

"In terms of the regulatory environment, around 240 bodies have signed up to the regulatory code. Some 15 of them are Tier 3 bodies, 50 plus are Tier 2 while 170 or more fall into the Tier 1 category. It's a good reflection of what's going on and a lot of work has been achieved in a relatively short space of time in advance of the statutory legislation. The sector is now used to being regulated and investors are very aware of this as it's an important consideration for anyone lending into the sector," he says.

While the emerging ecosystem is welcomed by AHBs, the borrowing capacity of the sector could be improved if it was allowed free up some of the existing mortgage debt on its balance sheet.

"There are limits to what some housing bodies can borrow but there are some mechanisms that could be improved by the Government that would help the sector to borrow more. If the sector could free up some of the current legal charges on its current stock, for example, some of which are tied up in non-repayable mortgage loans spread over for 20-30 years, this would go a long way towards improving the borrowing capacity of some AHBs," he says.

He also points out that the management performance of AHBs has also been strengthened over the past few years. Every year the ICSH publishes its Housing Association Performance (HAPM) report

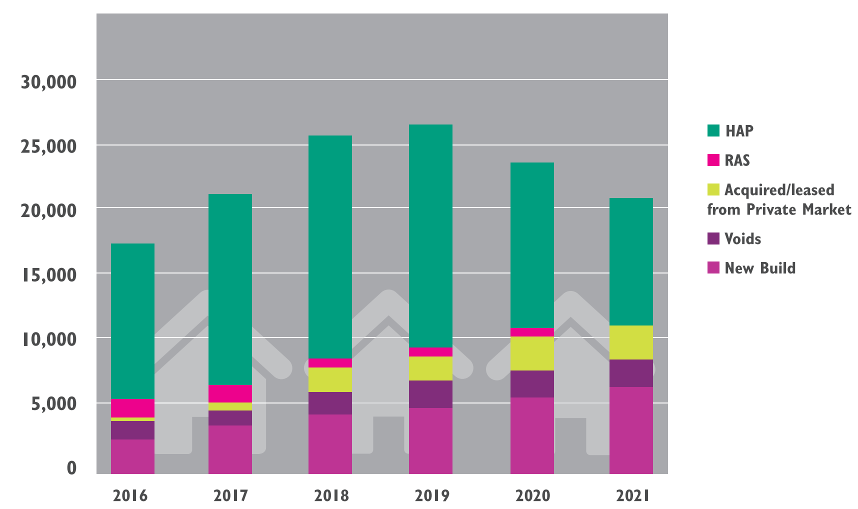
"Good management is key to preserving the long-term investment in social housing."

which provides key performance indicators covering areas like housing allocations, rent levels, service charges, arrears, voids and landlord tenant relations

"Good management is key to preserving the long-term investment in social housing and the most recent ICSH HAPM report for 2015 showed the results were strong in terms of things like rent collection, which was over 100%, including both current and previous rent arrears. Overall it shows that there was high demand for housing association properties and low turnover within the sector while it's also worth pointing out that there is a strong correlation between the condition and management of properties and the demand for them," he says

"Overall, the outlook for the sector is now very positive and there's a lot more collaboration, innovative thinking and a determined effort by all the stakeholders to deal with the housing crisis. Activity has increased dramatically and that's indicated by the amount of loan finance that has been approved as well as the number of schemes that have been approved by the Department. The focus is now ensuring that we deliver the targets set out in the Government's *Action Plan* and the social housing sector is keen to play its part," he concludes.

SPECTRUM OF SOCIAL HOUSING PROVISION FORECAST, 2016-2021



Source: Action Plan for Housing and Homelessness – Rebuilding Ireland.

RISK MITIGATION

Maura Moore examines how rent reviews built into state payments can impact on cash flow headroom over the cycle of project financing.

Maura Moore
Head of Professional Services and Nonprofits, AIB

The Government's *Action Plan for Housing and Homelessness: Rebuilding Ireland* commits to a range of measures designed to increase the supply of all forms of housing and further augment the ambition of Social Housing Strategy 2020. It calls for even greater collaboration between key stakeholders (Government departments and agents, developers, equity investors, banks, local authorities, approved housing bodies, landlords), in the delivery of 47,000 new social housing units by 2021 and supporting another 75,000 households through private sector delivery.

The Housing Agency has been allocated €70 million under the *Action Plan* and will target portfolios of distressed properties held by banks and investment companies, primarily private equity funds, to deliver social housing across the State. This gives a much needed supply boost to Approved Housing Bodies (AHBs) who are ramping up to deliver on ambitious growth plans and putting in place financing plans.

The Government's Capital Advance Leasing Facility (CALF), together with Payment and Availability (P&A) payments, have become one of the main funding mechanisms for the delivery of social housing. Support to AHBs is predicated on attracting private finance from commercial banks, the HFA and other sources of private capital including from reserves, and in turn meeting the Government's off balance sheet requirements.

Moreover, the funding mix is skewed in favour of private finance with the capital advance facility capped at 30% on an individual project. The P&A income stream up to a maximum 30-year term on a project by project basis affords repayment capacity to service debt finance and is attractive to AHBs and equity and debt providers alike. Any interruption to the income stream such as void or 'vacant' periods and rent reviews will have ramifications in attracting loan finance. AHB borrowers will need to demonstrate to finance providers how these risks are mitigated.

The Payment and Availability Agreement (PAA), a long-term contract for the availability of dwellings for social housing between local authorities and AHBs, provides for a rent review linked to an index of inflation every 3 to 5 years. As currently drafted the PAA rent review clause references the private rent sub-component index prepared by the CSO. Notwithstanding this, the Department of Housing, Planning, Community and Local

> *"The escalation of housing shortage to acute levels in recent years has led to much more rapid growth in rents than general inflation"*

Government has approved the use of rent review clauses linked to general CPI (consumer price inflation) in private landlord leasing arrangements. The average annual rate of rent price inflation was approximately 2.7% between 1996 and 2015. The equivalent figure for the overall CPI index was 2.1% over the same time period, with HICP (harmonised index of consumer prices) increasing at a slightly lower rate. (Note: The HICP for Ireland covers a subset of CPI components. The principal exclusion is household payments on mortgage interest).

Rent reviews linked to inflation will impact on the organisations' cash flow and debt service cover. Volatility is of no comfort to lenders and in particular where the debt term is in effect project lending sculpted in line with Government agreements. Lenders will move to mitigate these risks.

The historical evidence suggests linking to the private rent sub-component is likely to deliver higher State payments to AHBs. Current indications are that private rents prices will continue to increase more rapidly than overall CPI over the course of 2016 and 2017. Indeed, the escalation of housing shortage to acute levels in recent years has led to much more rapid growth in rents than general inflation and this is likely to persist for a number of years until we see a good pick-up in house building, which the *Action Plan* is aiming to alleviate.

However, linking to the rent sub-component introduces additional volatility to payment streams compared to income flows tracking CPI or HICP. This then suggests it is particularly important that AHB borrowers linking payments to developments in private rent prices are in a position to manage a period where State payments are reduced. State payments to AHBs would have been revised downward in 2012 on the basis of the average fall in rent prices over the previous four years (driven by steep declines in prices in 2009 and 2010). In contrast, were payments linked to CPI inflation and HICP these would have increased slightly over this period.

Figure 1 outlines the payment path to AHBs under each of the three indices based on reviews occurring every four years over a 20-year time period starting in 1996 (the majority of PAA rent reviews occur every four years).

For agreements tracking either CPI or HICP over the 20-year period above, each four-year review would have led to increased payments to AHBs.

It would seem therefore that a dampening of volatility may/will be required in a period of accelerated delivery, with both public and private financiers linking the PAA rent review clause to HICP in order to reduce/manage downside risk on state payments to AHBs.

For all social and affordable housing stakeholders who are contemplating sourcing development or project finance, on the back of robust business plans, contact AIB to see how best we can support your individual needs.

FIGURE 1: BENCHMARKED FOUR YEAR REVIEWS: 1996-2015

Source: Housing Agency

CASE STUDIES

Two customers of AIB share their views on the social housing sector in Ireland.

Seán O'Connor, **Túath**

With over 2,700 homes in twenty local authority areas under management, Túath is one of the country's largest approved housing bodies with an income of just over €10m in 2015. According to Seán O'Connor, Chief Executive of Túath, it is set to deliver 500 homes throughout Ireland this year with plans to exceed this number next year and subsequent years thereafter.

"It's probably fair to say that we have been the fastest growing association in Ireland over the last few years. This year in Dublin alone we will deliver around half of the voluntary sector's output of social housing in Dublin city, at a cost of around €46m," he says.

"We've had a busy year and we have geared up to respond to the challenges facing the sector by taking on new staff and doubling the size of our development and technical team. We will do our bit to ensure that the social housing targets set out by the Government are met.

"Our success has been built on private and public collaboration and I have no doubt that all our projects wouldn't have happened without collaboration between the State, local authorities, ourselves and the private sector," he says.

"The State can borrow for virtually nothing at the moment and a key thing for the sector is our ability to borrow from banks like AIB, or from international investors, because it's off balance sheet and doesn't count against public expenditure. It's important, because it allows more of the State's resources to be spent on hospitals and schools rather than housing. As long as the State facilitates us to borrow-and we have the capacity to borrow- it's a no brainer," he says.

"There's no point in building lots of houses for sale if ordinary people and working class families can't afford them."

"The State needs more social homes to break the vicious cycle of rising house prices and rents. The surest way to do it is to build sufficient homes, at lower rents, for families who really need them," says Seán.

But he cautions against building more houses for the sake of it, stressing that affordability should be the key influencer. "There's no point in building lots of houses for sale if ordinary people and working class families can't afford them. It won't curb escalating house prices and rising rents, it will simply drive more people into the private rental sector and further away from the prospect of home ownership."

He says that Túath is also looking at providing affordable housing to families who don't qualify for social housing but are priced out of ownership and the private rental market.

"Social housing is our core activity but we also want to help provide affordable housing to hard-pressed families in the squeezed middle market. The best way, we think, is for associations like Túath to work with local authorities and other associations to develop mixed tenure estates.

"While over recent years it's been cheaper for us to buy off builders rather than build ourselves, we are now changing our focus to construction, with developments on council land due to commence soon. The key to success on bigger sites will be to provide a mix of private, social and affordable housing. Any surpluses generated from the sale of housing will be ploughed back into our core business to provide more social and affordable homes. We see it as a natural extension of our existing activities," he says.

Peter Fenton, **Cill Dara Housing**

With over 140 properties under management, more than 40 of which are leased from the private sector, Cill Dara Housing Association (CDHA) is the largest AHB in Kildare.

A Tier 2 AHB with a strong track record that goes back to 1993, part of its mandate is to build communities, according to Peter Fenton, director of CDHA.

"While we are all about providing social housing, we also feel it's important to develop sustainable communities and this is something that some of the larger housing associations find it difficult to do," he says.

"Sustainable communities, and what goes on in them, are very important and we support a number of community initiatives on an ongoing basis. It's not a huge investment but they are important. But it's also about the people in these communities being able to support and contribute to them," he says.

"While we are all about providing social housing, we also feel it's important to develop sustainable communities."

The issues faced by CDHA are broadly the same as many other AHBs, he says.

"There simply isn't a ready supply of housing out there and the common consensus amongst other bodies in the county is that Kildare won't be able to deliver its target of 432 units by the end of 2017.

"Because we are so close to Dublin, there is pressure on pricing but also there's very little development taking place. There's plenty of sites but, for whatever reasons, developers are sitting on them and they seem to be slow in releasing them for development," he says.

While CHDA has over 40 houses under lease at the moment, the preferred route is to acquire units and it has in place bank finance, provided by AIB and supported by CALF funding, to allow it fund future acquisitions.

"We don't particularly like leasing as a model and we are now accessing bank finance. We have secured a €3m finance facility and we recently bought three houses and have another seven in the pipeline. For us it's currently cheaper and quicker to buy houses than to build and, for the time being at least, there's still good value to be had," he says.