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Financing affordable housing: A critical comparative review of the United Kingdom and Australia

PRIVATE INVESTMENT IN SOCIAL AND AFFORDABLE HOUSING HAS INCREASED SIGNIFICANTLY IN THE UNITED KINGDOM OVER THE PAST THIRTY YEARS. THE REVERSE IS TRUE FOR AUSTRALIA.

KEY POINTS

- Over the past thirty years, private investment in the provision of social and affordable housing has increased in the United Kingdom (UK) to £34 billion (A$92.67 bn) in 2003. This development has been important in changing the tenure structure of the housing stock towards growth in both home ownership and the not-for-profit housing sector, through housing associations.
- There has been a progressive decline in the proportion of the housing stock owned and managed by local government and funded by central government in the UK.
- The market for private finance has grown, in large part due to the robust financial regulatory structure put in place by the UK central government in a generally benign economic and policy environment. There are currently around 150 lenders, mainly large banks and building societies that lend to not-for-profit housing associations. The dual roles of the (central government created) Housing Corporation as both regulator and capital grant provider to housing associations has reassured private lenders while cementing political support for this policy direction.

This research is by ***Professor Mike Berry***, ***Professor Christine Whitehead***, ***Dr Peter Williams*** *and* ***Associate Professor Judith Yates*** *(AHURI Sydney Research Centre) through the AHURI RMIT-NATSEM Research Centre.* *The research explored the differences between the social and affordable housing sectors in the United Kingdom and Australia.*

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KEY POINTS

- There has been substantial private equity investment in home ownership, supported by policies such as allowing public tenants the right, and ability, to buy their dwellings at a discount price, through providing mortgage finance to low-income earners. Approximately £2 billion (A$5.45 bn) was invested per annum in this sector, in the UK.
- In Australia, to date, private investment has played a minimal role in providing affordable housing, in spite of ongoing policy debates and the canvassing of detailed models and approaches to the issue.

BACKGROUND

The United Kingdom

The expansion of private finance for social and affordable housing in the UK over the past twenty years was encouraged by a number of factors, including: the deregulation and liberalisation of the financial markets in the 1970s and 1980s; modifications to the land use planning system to encourage the provision of affordable housing; and the growth in central government supply-side subsidies (upfront grants) to housing associations and demand-side subsidies to low-income households.

By introducing a growing private finance market for social and affordable housing, UK policy makers and housing providers have effectively overcome a number of barriers. For example, the highly regulated structure of social housing has been replaced by a framework that provides a level of comfort to private lenders while increasing the housing associations' autonomy and potential to increase their financial and operating efficiencies.

In addition, the initial lack of understanding of the new market among private financiers – particularly as to the nature of housing associations – has been overcome, allowing a wide range of institutions to fund housing, particularly affordable housing. Originally, financial institutions lacked knowledge of and confidence in the social housing sector but, over time, as debt-to-asset ratios have increased, so too has market confidence.

In response, social housing management has become an increasingly professionalised occupation in the UK, supported by specialist training courses and professional development programs. This has substantially increased the effectiveness of the sector and improved the confidence of the financial sector.

The small scale and fragmentation of housing associations has been partly overcome by means of large-scale voluntary transfers of both properties and tenants, concentration of subsidies to larger housing associations, and the trend towards mergers and syndicates in the sector in order to increase economies of scale and borrowing power.

However, a number of changes in the finance markets and institutional environment may undermine the climate for private investment in affordable housing in the UK. These changes include the phasing in of rent control, increasing regulation of housing associations, and decreasing numbers of stock transferred from local authorities to housing associations.

Australia

Social housing policy reform in Australia has largely been confined to internal changes to the dominant policy and funding vehicle, the Commonwealth State Housing Agreement, through which social housing has increasingly been targeted at specific, high-need groups, such as the disabled and sole parents.

Private investment has played little part in the provision of social housing in Australia. State and territory governments, in particular, have generally been unwilling to transfer public housing stock, and the existing community housing sector is very small. Further, the real value of supply-side subsidies to public housing has fallen consistently over the past decade, and this, coupled with the increased targeting of available stock to people with low incomes and multiple disadvantages, has put the State Housing Authorities under substantial financial pressure.

METHODOLOGY

The project undertook a selective review of relevant existing studies focusing on the role, presence and impact of private investment on affordable housing provision in the two countries, as well as relevant policy documents (mostly unpublished) and government statements.

The researchers also conducted targeted interviews with key players in the government, community and financial sectors, to test and supplement the information derived from the literature review. These interviews (in both the UK and Australia) were with players who have had, or were likely to have, an influence on policy interventions.

KEY FINDINGS

The shift in policy focus, through targeting and allocation policies and a decrease in funding levels, in both the UK and Australia, has redefined the role of government, placing constraints on traditional loan and tax sources of funding for social housing. This has led to an interest in leveraging private equity investment into the provision of affordable housing to low-income groups.

The intervention of private financing in the provision of affordable housing in the UK has had substantial influence.

- Cumulative investment exceeded £34 billion (A$92.67 bn) by 2003. Although annual investment in this sector has declined in recent years, it is still over £2 billion (A$5.45 bn).
- The private finance market consists of about 150 lenders, mainly UK-based large banks and building societies that lend to housing associations of varying sizes.
- Intervention is heavily directed towards mortgage lending, but a growing bond market is emerging for the debt of the larger housing associations and syndicates of smaller associations.
- In addition to funding 40–50 per cent of the cost of new housing association construction, private investment has financed the transfer of about 900,000 dwellings[1] from local authorities to the housing associations and some two million dwellings under the 'Right to Buy' legislation, introduced in 1980.
- More recently, a number of shared equity/ownership schemes for low-income people have been introduced through housing associations. These schemes sometimes include housing association equity, and sometimes only involve private loan facilitation supported by a government subsidy, with the residual finance provided by private mortgage lenders.
- Targeted support by way of direct grants to 'key workers' has been used to address labour market concerns in particular regions, notably the south-east of England. In each case, private mortgage lenders finance the balance required after the government subsidy.

A number of barriers still exist and may affect future flows of private investment into affordable housing in the UK.

These include:

- The demand for affordable housing varies across regions in both countries. Some areas have excess affordable housing, particularly in those inner city areas with multiple social problems and poor quality stock, where private investment and regeneration could have major social benefits but where risks are also high, dissuading private investors or significantly raising the price of private finance.
- In the Australian context, lenders' willingness to be exposed to this low-return investment market may be constrained by the likely future emergence of alternative lending opportunities (such as 'non-bank lenders') and, in the wake of major changes to the rules of international banking, the increased flexibility in a competitive financial market.
- The political risk related to rent and subsidy policies, regulatory arrangements and taxation arrangements may cause investors to withdraw or re-price their involvement in these markets. This may mean that rents and purchase prices are increased to meet investment costs, thus rendering the housing unaffordable.

Most of the barriers identified in the UK, including those that have effectively been overcome, exist in Australia, within the complex political context of Commonwealth/state/territory relations.

POLICY IMPLICATIONS

There has been lively debate over the past few years as to how substantial volumes of private finance could be leveraged into affordable housing in Australia. The following approaches have been suggested:

- Consortium model – a capped Commonwealth government subsidy to the states and territories would enable the latter to borrow from private finance institutions and acquire dwellings to rent to low–moderate income households at income-related rents.
- Retail investment vehicle – retail equity investment would be pooled for the acquisition of rental dwellings managed by community housing organisations. However, substantial government subsidies would be required to deliver the required return to investors and provide affordable rent to tenants.

1 *The transfer-to-housing association market is dominated by a small number of large lenders, typically providing finance in tranches of £50 million or more.*

- Tax relief for retail investors renting to community housing organisations – special tax benefits would be directed at private landlord/investors who rent their dwellings, on long leases, to community housing organisations or other not-for-profit providers for a minimum period of time.
- Low income tax credit scheme – in similar manner to the US scheme, most of the benefit would be targeted at landlords who provide lower-cost rental dwellings, thereby encouraging private investment in that sub-market.
- Capital gains tax partial exemption on the sale of affordable rental dwellings – most benefit would be delivered to investors who provide affordable rent stock, and this, arguably, would encourage private investment in that sub-market.
- Shared equity model – institutional investors would be able to buy an equity share in a mixed pool of dwellings across the states and territories. Private equity investors would receive their return in the form of a share in the growing capital value of the dwellings.
- Providing housing associations with a strong regulatory framework, funding and capacity-building opportunities would enable them to form workable, mutually beneficial relationships with private financial institutions.
- Affordable housing in Australia would be better supported through a flexible planning system similar to that in the UK, which mandates private developer contributions to affordable housing outcomes.

FURTHER INFORMATION

This bulletin is based on AHURI project 30206, *Financing affordable housing: A critical comparative review of the United Kingdom and Australia.*

Reports from this project can be found on the AHURI website: www.ahuri.edu.au

The following documents are available:

- Positioning Paper
- Final Report

Or contact the AHURI National Office on +61 3 9660 2300.

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