POLICY EVIDENCE SUMMARY

February 2018

Will social impact investing supply affordable housing in Australia?

Summary of AHURI Final Report No. 294: Understanding opportunities for social impact investment in the development of affordable housing

AHURI
Australian Housing and Urban Research Institute

What this research is about

This research is the first to examine the opportunities for, barriers to and risks to social impact investment (SII) for social and affordable housing in Australia.

SII aims to achieve a specific beneficial social objective together with a financial return, and measure the achievement of both. Through collaboration between service providers, investors and governments, SII can untap new sources of capital (through accessing different types of investors) and enhance the return on government investment.

The context of this research

While SII is increasingly of interest in relation to homelessness and housing vulnerability, its application to affordable housing supply has not attracted the same kind of policy attention. Little therefore is known of investments, the size of investments, who the investors are, their motivations or the impact arising from their investment.

The key findings

The demand for SII funds

The largest demand for SII funds for social and affordable housing is from community housing providers (CHPs), which make up the only established system that meets the requirements for verifiable impact over time.

The largest share of SII in social and affordable housing is from banks to CHPs, and is estimated to be in the order of $1.5 billion dollars. Another $20 million dollars was invested in non-community housing models by non-bank social impact investors.

How SII operates

SII funds are placed directly by investors or through intermediaries who specialise in SII funding. Intermediaries take responsibility for measuring and reporting the impact investments achieve.

The return expectations of investors can differ: from 'impact-first' investors who are willing to accept concessionary returns (i.e. a below market return) to 'finance-first' investors who require non-concessionary returns equal or near equal to market.

Investment deals can be complex, involving other SI investors, concessionary and non-concessionary investment, non-SI investors and philanthropic and other grants. Such deals are termed 'layered' investments. Investment can involve debt, equity or both.

Who are current social impact investors in Australia?

Through their lending to CHPs, Westpac Banking Corporation, Community Sector Banking and Bank Australia are the largest investors in social and affordable housing in Australia, with Westpac having $1.05 billion invested in the CHP sector. Total bank SII investment in the CHP sector is possibly as much as $1.5 billion at present. This investment is all debt investment, and returns are non-concessionary.

Historically, access to capital has been difficult for CHPs and investment has required reconsideration of risk and a shift in credit assessment. The participation of banks in SII adds competition to the market, ensuring all CHPs gain more competitively priced capital and more suitable conditions on finance. For these reasons, banks therefore could be said to be providing 'additionality', or added benefit to the SII market.

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Figure 1: Categories of Australian social impact investment strategies

Full impact-first	Full finance-first
• Concessionary returns • Reformed credit assessment	• Non-concessionary returns • Orthodox credit assessment
Partial impact-first	**Partial finance-first**
• Concessionary returns • Orthodox credit assessment	• Non-concessionary returns • Reformed credit assessment

Source: AHURI Final Report No. 292

A further $20 million is invested in housing models outside of the registered CHP sector by non-bank investors. These include the Lord Mayors Charitable Foundation—who provided $3 million to the Affordable Housing Loan Fund, small superannuation funds, high net worth individuals, other individuals, philanthropy, self-managed super funds and not for profit organisations. This $20 million is equal parts debt and equity investment. The equity investors in these models were the only investors to accept concessionary returns. They were supporting innovative models that have the potential for systemic change rather than simply providing housing.

Who are the Intermediaries?

Three intermediaries—Foresters Community Finance, Social Enterprise Finance Australia and Social Ventures Australia—are currently responsible for the placement of the majority of non-bank SII in social and affordable housing in Australia.

These three intermediaries are highly respected and were established following an Australian Government initiative, the Social Enterprise Development and Investment Funds that provided $20 million in matched funding. Christian Super recently established its own intermediary, Bright Light.

Intermediaries have attracted funds from high net worth individuals, NAB, Triodos Bank, Community Sector Banking, Christian Super, HESTA and the NSW Aboriginal Land Council.

Government assistance is regarded as necessary to grow the CHP sector and enable SII at a greater scale.

Categories of Australian social impact investors

In Australia, SII in social and affordable housing does not fit a simple 'impact-first' versus 'finance-first' investment strategy. Rather, the research finds most investments can be described as 'partial finance-first' reflecting a combination of non-concessionary returns and modified investment parameters. A far smaller proportion is 'fully impact-first', in that concessionary returns were accepted and investment parameters were modified. There is no evidence of fully finance-first or partial impact-first investment.

Social impact investors have reconceptualised risk and modified their lending practices in addition to consideration of return requirements. This is not a case of accepting greater risk but rather of reviewing the generally accepted credit assessment practice.

Barriers to SII

The gap in funding between tenants' capacity to pay and the cost of provision is the most significant barrier to SII.

The opportunity for SII is also limited by CHP sector constraints, including limited free cash flow (to support borrowings); uncertain tenant housing assistance and income support; and reduced discretion over tenant allocation.

Government policy change is viewed as a key source of risk affecting investment. Adverse changes to welfare and housing assistance, and government policy restricting housing allocations to the highest priority applicants on public housing waiting lists were identified as affecting CHP cash flow, presenting a risk to investment.

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What this research means for policy makers

SII in social and affordable housing does rely on government commitment in the sector. Private SI investors expect returns on their investment. Investment therefore only occurs when the CHP is able to generate a positive cash flow to support debt repayment or disbursements to equity holders. This requires the gap between tenants' capacity to pay and the cost of housing provision to be funded by government. The funding of this gap provides an implicit government guarantee.

Government assistance is regarded as necessary to grow the CHP sector and enable SII at a greater scale. In Australia, this may include:

Figure 2: Policy options to grow community housing and enable social impact investment at scale

- an annual funding stream for CHPs to close the gap between rental revenues and cost of provision
- state and territory governments to allow CHPs discretion in who they house so that investor confidence can be maintained (in the absence of a funding stream to meet the gap between rental revenues and cost of provision)
- an annual capital grants program for CHPs to grow the sector
- growth of the sector to create the conditions for bond financing—bonds lower the cost of capital and provide for long tenure debt
- welfare entitlements and housing assistance to provide sufficient income to ensure the most vulnerable households will be attractive to house. Social security entitlements need to be stable in order to provide confidence to investors regarding their existing investments as well as future investments
- well-located, government-owned land that is surplus to requirements could be granted to CHPs to help develop affordable housing
- inclusionary zoning could be implemented to provide a new source of social and affordable housing on existing redevelopment sites. Inclusionary zoning would provide the opportunity for layered investment models, common in the US
- governments could consider capturing the uplift in value when re-zoning land, through making part of rezoned sites available to CHPs or other NFP housing providers.

SII in new home ownership models is able to generate affordable housing supply for both low-income and intermediate income cohorts. The growth of some of these models could be assisted through:

- government guarantees to permit debt financing and negate the need for substantial equity contributions
- funds to provide equity to development projects that would be returned once mortgage loans are issued.

SII would be assisted by government providing legal clarity for superannuation funds investing in concessionary SII projects.

Methodology

This research reviewed national and international literature on SII in affordable housing and interviewed experts in government, social impact investors, intermediaries and CHPs.

Further information

NOT FOR CITATION. TO CITE THE AHURI RESEARCH, PLEASE REFER TO:

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