INSIDE HOUSING

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A perfect match

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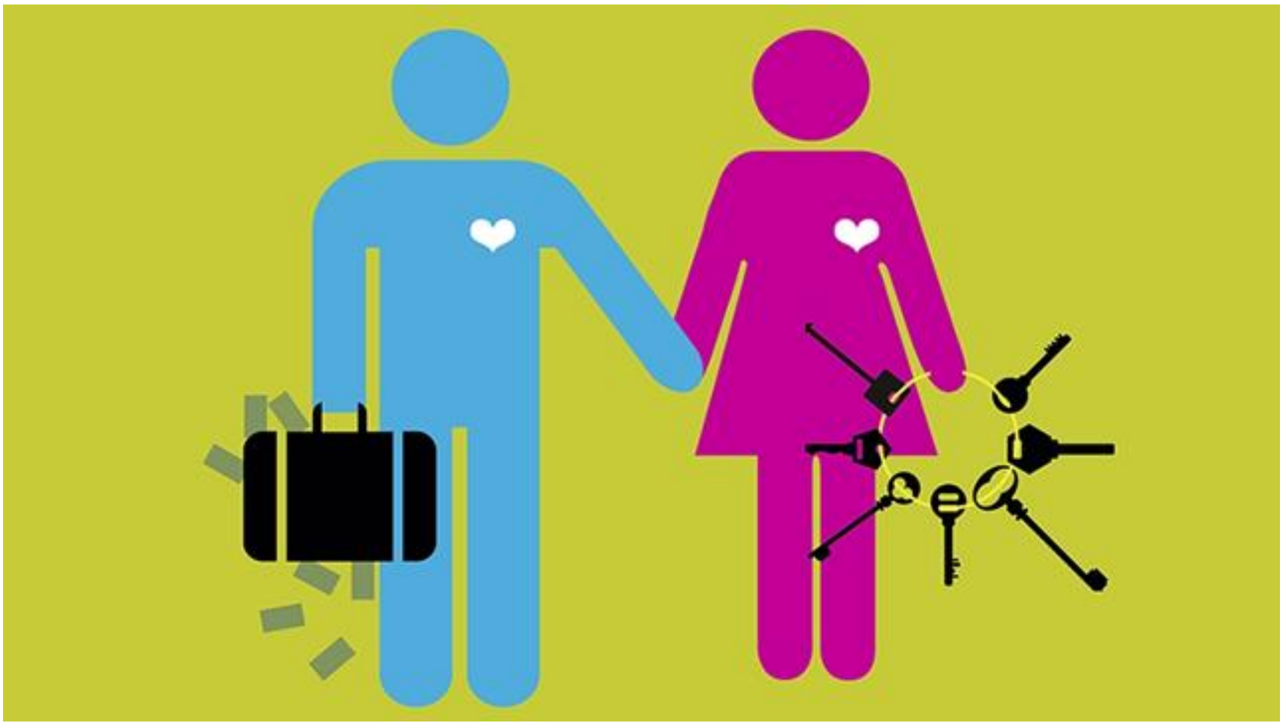

As government grant and bank loans play hard to get, housing providers are struggling to get funding for development. But, as Austin Macauley finds out, the sector has caught the eye of capital investors

There's good news if you're a social landlord in search of new funding - investors are driven wild by your assets.

Indeed, the sector is currently such an attractive proposition that one investor told Simran Soin, finance director at Places for People, that his peers are 'desperate' to hook up with housing associations.

'He said they are desperate for new entrants from this sector to invest in,' Mr Soin recalls. 'There's a significant amount of money out there that investors are looking to place in this sector. It's about organisations going out and getting it for themselves.'

At a time when government grant is falling and banks are less willing to lend, this should be music to the ears of housing associations looking for cash to push forward with their development plans.

Then again, 'go and get it' is easy to say when your organisation - with 81,566 homes - dwarfs the size of most landlords and has raised somewhere in the region of £1.5 billion from capital markets since the 1990s.

Mr Soin accepts PfP has the capacity, clout and know-how to access a variety of forms of finance, but he believes investors are hungry for new opportunities and the market is opening up to smaller housing associations.

Evidence of that trend is in plentiful supply. Last year around £4.4 billion was invested in social housing via public and private placement bond issues, bringing the total for the sector to £12 billion by December 2012 - 14 per cent of the entire long-dated bond market in the UK. Even allowing for the fact that 2012 was a bumper year, investment in the sector remains on course to continue growing annually by at least £1 billion.

So what are investors looking for in a social landlord? Ask investment managers such as M&G, Legal & General and Aviva what ticks their boxes and you'll get largely the same answers. Does the organisation have a sound financial record? Are its assets well managed and in good condition? Is that asset base likely to diminish due to right to buy? Does it make a reasonable surplus to service the interest and ultimately repay the debt? Does it have a quality management team?

Dating strategy

Mervyn Jones, director of housing at Savills, says many investors want to see an active asset management strategy - one that goes beyond simply maintaining the stock. It will identify properties to dispose of, for example, because they are no longer fit for purpose or have high value that could be realised and reinvested.

'What can you do to prepare yourself? Get your asset register, records and contingency plan up to date for when you are presenting to investors,' says Mr Jones.

On average, landlords have to put up three properties as collateral to secure investment in every home they build. Joseph Carr, finance policy leader at the National Housing Federation, says the ratio has risen due to falling government subsidy and warns some 'are running out of capacity'. But he believes there is untapped potential, particularly among stock transfer landlords, many of which have spent their first years focusing on bringing their homes up to a good standard, and now have assets that are of a high enough quality to make them an attractive investment proposition.

Medium-sized landlords are particularly catching the eye of investors. At the end of September, 11,000-home Knightstone Housing Association announced it had sealed a £100 million private placement to help fund its plans for new affordable homes.

Whereas in previous years housing associations would need to be seeking upwards of £50 million to access capital market finance on their own, those thresholds are falling. Investors like M&G, which manages £3 billion of investment in the sector, will now go as low as £10 million per transaction.

A good catch

This appetite can partly be explained by the nature of social housing organisations. They have long-term assets matched with a long-term commitment to the area they work in, a steady rental income from tenants that is index-linked, they are regulated and have government backing in the form of housing benefit.

'These organisations are not like housing builders, here today and gone tomorrow,' says Mark Davie, head of social housing at M&G. 'Even if they get taken over or merge with other housing associations, the housing will still be there. We like stable, predictable cash flows.

'A good proportion of that income stream is underpinned by welfare [benefits], therefore the quality is quite high. No one has actually lost money to this sector.'

Background research

As investment in the sector has grown so too has investors' knowledge. The boom in 2012 was in part down to housing associations going to market following the announcement of the £4.5 billion affordable homes programme for 2011/15.

Piers Williamson, chief executive of the Housing Finance Corporation, a not-for-profit organisation offering loans to housing associations using funds raised by issuing bonds to private investors, says the volume of bond issuance last year has encouraged investors to 'put a lot of time into understanding this sector'. The more they get to know it, the more they want to invest and, at present, demand is outstripping supply.

This year's spending review clarified the funding situation further with the £2.8 billion affordable homes programme for 2015/18 and the 10-year rent settlement for social landlords. As a result, the expectation is there could be a boom to match 2012.

'There's a whole raft of housing associations - small and medium sized - that are about to come to market,' says Adrian Carter, head of banking and finance at law firm Trowers & Hamlins. 'There's been an element of registered providers sitting there, hoping the banking market will come back to where it used to be and realising it's not going to happen soon. They're looking for alternatives and capital markets are the obvious one.'

In recent months the sector has been hit by credit rating agency downgrades and the repercussions of welfare reform in the shape of soaring rent arrears. Yet this has done little to dent investor confidence. Both M&G and Aviva believe the government loan guarantee scheme has been enough to reassure capital markets that it will remain on-hand should things go wrong.

The government's 'something for something' mantra requires landlords to sweat their assets in return for grant funding, and they are increasingly going to capital markets to raise investment for broader development projects as a way to cross-subsidise below market rent housing.

Waqar Ahmed, director of finance at 77,000-home L&Q, explains how half of the organisation's new homes are for sale and the remainder are for below market rent.

He believes the whole sector can play its part in boosting housing numbers. 'I don't accept that only large developers can contribute to development of affordable homes. It's about opportunity and being prepared to take risk,' he says.

L&Q has been in talks with London's small associations to look at how it can help them build new homes. Possibilities include match-funding and offering its resources and expertise to raise private finance.

False impressions

It's a sentiment echoed by PfP's Mr Soin, who argues too many people have built the task of accessing capital markets into 'some kind of mythical beast'.

'It's not as hard as people think it is,' he says. 'Some barriers have been broken down - certainly those barriers with investors, who are now more comfortable with the sector.'

While the wholesale bond market - which is defined by the London Stock Exchange as bonds tradable in units of £50,000 or more - may still be off-limits for smaller organisations, he believes retail bond markets - which were created by the London Stock Exchange in 2010 in order to attract a wider range of investors - are a viable option because they offer the chance of finance in 'smaller chunks', often of around £1,000.

'The best thing to do is seek advice from those who have already trodden that path,' he adds. 'Find out what practical steps need to be taken if you're preparing for an issue in the markets, who you need to talk to, etc.'
And if you follow all those steps you might just find the perfect match.

Knightstone's deal

At the end of September Knightstone Housing Association secured £100 million through a bond issue and became the first social landlord to do so without having to secure a credit rating. The landlord believes it's a sign of confidence in the sector as a whole as well as in its own organisation.

Knightstone, which manages 11,000 homes in south west England, structured the deal so it can access the funds when they are needed. It has drawn down £1 million initially and will take a further £49 million in 2017 to help pay for its development programme of affordable homes, which has yet to be finalised. The remaining £50 million has been retained to sell to investors in the future.

Rather than issue a public bond, Knightstone opted for private placement, which gave it added flexibility and allowed it to defer accessing the proceeds - saving £3.6 million in the process.

Duncan Brown, director of resources at Knightstone, describes the path towards securing debt finance as 'quite a formulaic process' but involving 'incredibly intense work'.

The guarantee scheme

When the government announced the Housing Finance Corporation would run its £3.5 billion loan guarantee scheme in June, it effectively gold-plated the message it sent out to investors.

For the past 26 years THFC has given smaller housing associations access to capital markets, borrowing itself and lending on to landlords. To date, the not-for-profit organisation has raised around £1.5 billion of investment.

Its latest deal in October raised £81.5 million for nine associations via a tap on its social housing bond with amounts borrowed ranging from £17 million to just £3.5 million. For the social landlords involved, such as 750-home Soho Housing based in central London, it ensures a flow of private finance for new development.

Piers Williamson, chief executive of THFC, says the deal - at 4.5 per cent over 30 years - compares favourably with those struck by the largest housing associations.

Readers' comments (1)

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  ManWithAbacus | 14/11/2013 2:48 pm

  As anyone who has dated will attest... sometimes the only thing the other person is interested in is your assets.

  They would like you to be engaging, well behaved, clean and presentable, however, they only really want one thing - a return on their investment.

  Offers of "gifts aplenty" and "quiet secluded engagements" are fine but beware... these are professionals... they are paid to perform at your expense.

  Mismatched deals like those reportedly done by Genesis - RPI funding against market rent - are a blight that could plague an organisation for years to come.

  As with any form of dating... know what your getting into... think safety... meet in the open... don't get carried away