Affordable homes: opportunity knocks

Ruby Giblin and Matt Cowen consider how recent industry changes – including on the right to buy – are affecting local authority development programmes

Following the removal of the Housing Revenue Account (HRA) debt cap in October 2018, many local authorities are using their new found borrowing powers to accelerate development programmes. However, in order to take full advantage of this new freedom, local authorities should take note of recent industry changes and consider how these may impact development plans. Three are highlighted here: changes to the right to buy regime, changes to the Public Works Loan Board (PWLB), and shortages of skilled staff.

Right to buy

From 2012 local authorities were granted powers to re-invest right to buy receipts for the provision of social housing. However, practical problems have since emerged around how to re-use these receipts, particularly given that they cannot constitute more than 30% of the development costs. Local authorities are therefore finding that they still hold receipts after three years and face having to pay them back to the Treasury with interest.

Local authorities have therefore been keen to find methods to maximise their use of right to buy receipts but this has not proved straightforward due to restrictions on transferring right to buy receipts. The most problematic of these is not being able to transfer them to a body in which local authorities have a "controlling interest" which captures traditional local authority-backed development companies.

This is now leading local authorities to seek creative solutions. Many local authorities are setting up new independent community benefit societies in which the local authority has no controlling interest to develop sites which can then be gifted right to buy receipts. Local authorities can still retain some control by ensuring that the rules of the society cannot be changed without local authority consent or by loaning money to the society subject to strict loan covenants and conditions.

Some local authorities are also setting up housing delivery partnerships with housing associations or private companies in order to deliver social housing. For this model to succeed, the partners of the venture, who may have very different objectives, must be clear about each of their objectives and take care to adopt an appropriate corporate structure to reflect this.

The feedback to the government's 2018 consultation paper on use of right to buy receipts is still being analysed but the paper hinted that there may be changes afoot.

Changes to PWLB rate

Local authorities need more grant funding and the Chancellor's £12bn gift is welcome. However, in addition to grants, PWLB monies allow all local authorities to borrow at the same rate (if central government chooses to lend). The onerous 1% rate increase that was imposed last year has been removed (for building social housing only), but may still apply for non-social housing borrowing. Previously local authorities' activities included wholesale borrowing to fund commercial enterprises and taking risk (picked up by council tax increases) which will continue to attract the higher rate. Private equity houses, which could just about compete with the increased rate, have now been out-manoeuvred by the Chancellor if they were considering investing in social housing.

To date, very few local authority bond issues have taken place because of freely available PWLB loans (depending on the creditworthiness of the local authority involved); the rate cut means that it remains difficult for them to compete, although there was evidence that conversations had started with the private sector, particularly following the issue of the £350m UK municipal bond, but these may no longer be sustainable if their focus is funding social housing.

As it stands, local authorities are likely to continue to look to the PWLB (now within HM Treasury auspices). For a financially savvy local authority, monies are handed out without too many questions in a matter of days, without long negotiations over terms and conditions. The private sector will only be interested in the same demographic, that is, certain creditworthy local authorities and not others. There would have to be very distinct market advantages for such local authorities to jump ship; the slash in the PWLB rate will not help the private sector. Moody's believes that the PWLB will continue to prevail for a majority of councils for some time.

Skilled staff

Post-Brexit, will shortages of skilled staff in construction slow down the rate of homes being built by alternative methods?

Generally, for modern methods of construction (MMC) fewer construction workers are required but they require different skill sets. Government initiatives are looking for the MMC sector to deliver another 80,000 jobs, mostly in the North. For example, Ilke Homes is employing and training 800 people from local communities having received £30m of grant from Homes England to stimulate jobs and production in the northern corridor.

The MMC sector offers career opportunities in various disciplines not usually associated with construction - being in a warm factory and not on site for very long, and specific MMC qualifications are in the pipeline. MMC is a chance to create a new industry, and revive communities, such as the Ilke Homes factory that replaced the Yellow Pages factory.

Perhaps we are asking the wrong question about MMCs. What is actually slowing down the rate of houses being built is availability of funding, acceptability of building warranties, and the initial cost of production, which is at least 12% more than conventional construction for housebuilders. Readily available finance would unlock this, enabling some traction and economies of scale to gather pace, and for MMC to create a sustainable and thriving industry fit for the 21st century.

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