

MILLIMAN DISCUSSION PAPER

Financing social and affordable housing

The potential role of pooled investment funds in helping alleviate Ireland's affordable housing crisis

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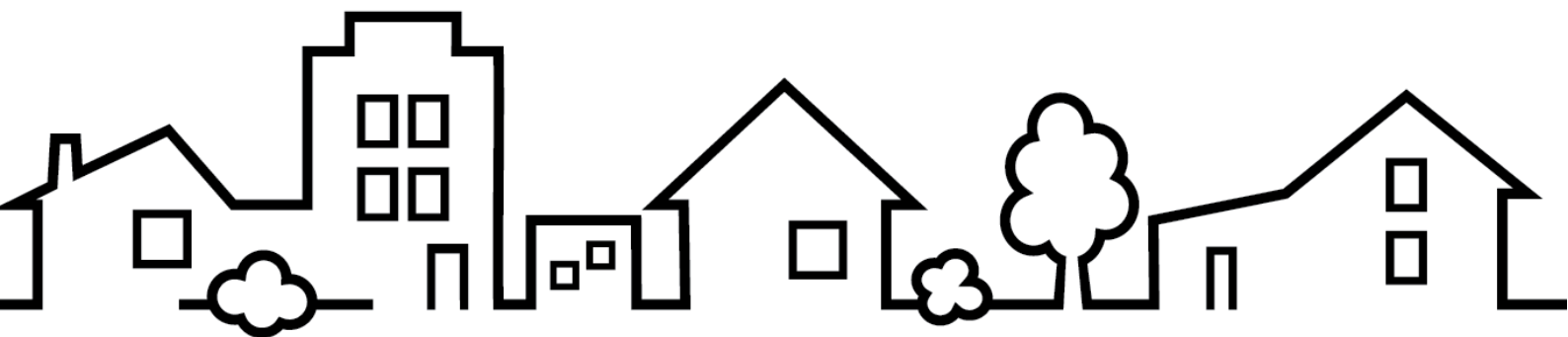


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Authors, acknowledgements and background

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BACKGROUND

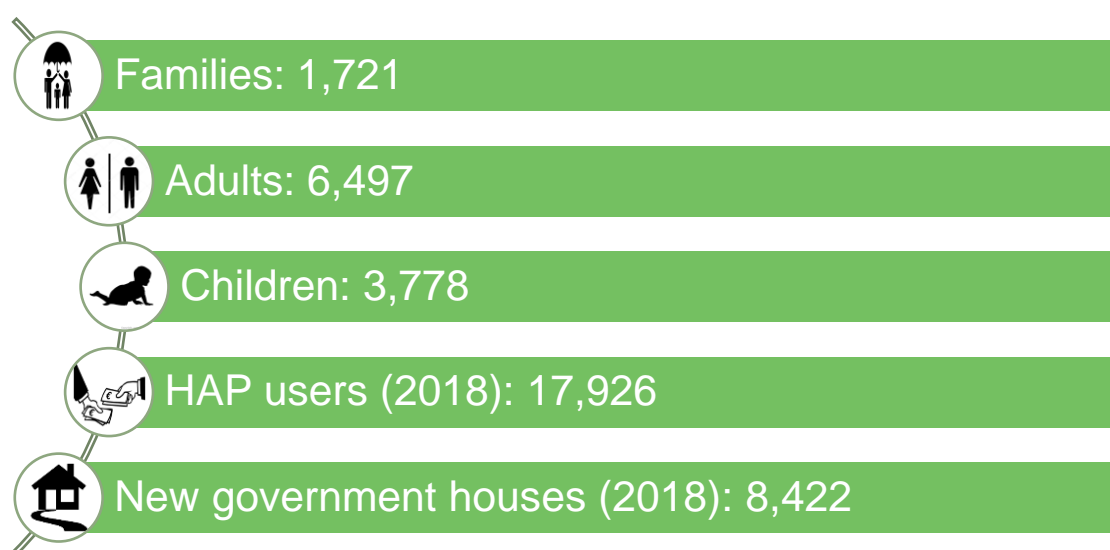
This paper is arguably a departure from a 'normal' actuarial research paper. It steps outside our traditional area of operation and expertise and is an attempt to explore how the financial services industry could help address a wider societal challenge like homelessness. The paper has been produced as part of our wider efforts in relation to corporate social responsibility (CSR) and reflects Milliman's mission to serve our clients to protect the health and financial well-being of people everywhere.

The ideas set out in this paper are intended to be a starting point for a discussion on how pooled fund investments could provide a source of funding aimed directly at social and affordable housing. The expertise required to develop these ideas further extends beyond our subject matter areas, and includes legal expertise, economics and investment management, as well as the contributions of those actively involved in providing services to families in homelessness. Therefore, the paper calls for collaboration and input from others who have the right expertise and are willing to share it. The paper raises questions, without fully providing answers. We acknowledge fully that this is a complex issue and that we are not subject matter experts in the topics raised, and we encourage those reading the paper to share their thoughts on whether, and especially how, this proposal could be refined to make it more effective.

1. Introduction

Ireland is in the midst of an affordable housing crisis. Figures published by the Department of Housing, Planning & Local Government show 6,497 homeless adults in late July 2019 with a further 3,778 homeless children. In total 1,721 families were in emergency or temporary accommodation including hotels, bed and breakfasts (B&Bs), hostels and other temporary accommodation facilities.¹ In addition, a large number of people are in private rental accommodation, relying on local authority assistance in paying rent. By end 2018, 17,926 people were benefitting from the Housing Assistance Payment (HAP) with a further 755 people supported by the longer-term Rental Accommodation Scheme (RAS). Through building activity, acquisition and leasing, the government's social housing stock increased by 8,422 houses in 2018,² but with the continued huge demand for housing services and support, it is difficult for the state's infrastructure to keep pace with demand. Statistics issued by the Housing Agency for 2018 showed a reduction from June 2017 to June 2018 of almost 14,000 in the number of households on the social housing waiting list. The number of households remaining on the list was almost 72,000.³

FIGURE 1: HOMELESSNESS IN IRELAND



Tackling the number of families in emergency accommodation, and providing support for individuals and families struggling to find affordable rental accommodation is clearly a significant challenge, albeit one that is high on the political agenda. The issue is clearly a high priority for the general public too—if column inches and crowd numbers at housing protests are a reasonable benchmark.

The root causes of the housing crisis are manifold. A shortage of housing supply appears to be at the crux of the problem, particularly in the context of increased demand arising from improved economic conditions and an increased number of large multinational employers. In addition, media commentary has pointed to vacant properties, some owned by local authorities, as well as short-term rental properties through Airbnb and similar organisations depleting supply further.

A detailed analysis of the background to, and causes of, the current housing crisis is beyond the scope of this paper. However, we believe that increased financing, focused directly on social and affordable housing, can play a significant role in alleviating the crisis. We acknowledge that such a solution will not necessarily, on its own, solve the supply-side challenges in the housing market, or other wider issues. However, we believe it could play

¹ Department of Housing, Planning and Local Government. Homelessness Report, July 2019. Retrieved 9 October 2019 from https://www.housing.gov.ie/sites/default/files/publications/files/homelessness_report_-_july_2019.pdf

² Department of Housing, Planning and Local Government (2016-2019). Overall Social Housing Provision. Retrieved 9 October 2019 from <https://www.housing.gov.ie/housing/social-housing/social-and-affordable/overall-social-housing-provision>.

³ Housing Agency (September 2018). Summary of Social Housing Assessments 2018. Retrieved 9 October 2019 from https://www.housing.gov.ie/sites/default/files/publications/files/summary_of_social_housing_assessments_2018_-_key_findings.pdf.

a significant role in helping to reduce the numbers of families in emergency accommodation, and provide additional housing options for those struggling to find affordable private rental accommodation.

For an individual member of the public with strong feelings on the importance of tackling this crisis, the potential courses of action available are not immediately evident. Charitable contributions can, and do, make a difference. Letters to politicians and contributing to increased political pressure may also be effective, but for many there is likely to be a sense that an individual has limited capability to have a meaningful impact on an issue of such magnitude.

We believe that harnessing the power of pooled investment funds could be a way for individuals, companies, investors and larger financial institutions to direct meaningful financing specifically targeted at social and affordable housing in a way that could significantly alleviate this crisis while also potentially providing returns to individual investors.

In summary, the proposed pooled investment fund would:

- Build a portfolio of residential properties, through acquisition and/or development. Initially, it is likely that the focus of the fund would be on purchasing residential properties, but development of suitable residential properties would also be possible over time.
- Rent those properties on long-term secure tenancies with transparent rules around rental increases either to tenants directly in receipt of the HAP or directly to local authorities to supplement the local authority social housing stock.

In this paper we set out the rationale for a pooled investment fund focused on social and affordable housing. In particular we identify the potential for such a fund to allow smaller contributions by individual investors to collectively achieve greater outcomes through pooling of resources. Contributions to the fund would be investments, rather than charitable contributions. This would provide all investors with a share in a portfolio of social and affordable housing that has the potential to provide attractive returns. A clearly articulated set of governing rules and principles for the fund would ensure that all investors are clear how the fund will operate, and what its focus will be from a social and affordable housing perspective. Clear governance will allow investors to understand how the fund is being run, including what costs and expenses are being incurred. This will ensure that investors can make a clear and informed decision, generate a potential return and help tackle the social and affordable housing crisis in the process.

Having a pool of residential rental properties that focus solely on the social and affordable housing market will help alleviate the supply challenges that individuals and families in that market are facing. In addition, a focus on long-term secure tenancies could play a crucial role in providing security of tenure, which would remove a key challenge currently faced by HAP scheme renters.

These are strong aims, but we believe they are achievable through a pooled investment fund structure. However, a range of hurdles must be overcome to convert an idea of this nature to a reality. A successful launch of a pooled investment fund of this nature would require the collaboration and assistance of a range of parties with relevant expertise, including legal, economic and investment expertise on the one hand, and on the other close working knowledge of the housing crisis, the work of homeless charities and the relevant government agencies.

The purpose of this paper is to set out the concept of a pooled investment fund targeted at social and affordable housing. We intend to introduce our ideas on how such a fund might work. In the process we will identify some potential pitfalls, or at the very least challenges which we think may need to be overcome. This paper is intended to form the starting point for a discussion. We acknowledge that we do not have the expertise to tackle this challenge ourselves, and invite others to collaborate, discuss and challenge as appropriate with a view to collectively building something stronger.

2. Social and affordable housing

In this paper we use the term social housing to mean housing that is provided directly by the government or local authority to individuals, typically based on criteria defined by the government or local authority. Social housing can be built or acquired by local authorities or alternatively can be rented directly by the local authority. In the context of the proposed pooled investment fund, the social housing component refers to rental properties owned by the fund and rented to the local authority for social housing purposes (generally at slightly below market rates). Local authorities operate social housing waiting lists and individuals who qualify (through means testing primarily) are added to the waiting lists in the relevant geographic areas.

Affordable housing, in the context of this paper, relates to properties rented directly to private individuals who are in receipt of rental support from the government or local authority. Two primary forms of assistance are available—the Rental Accommodation Scheme (RAS) and the Housing Assistance Payment (HAP). The HAP is a far more common form of support. Given the low relevance of the RAS in this context, we have not focused on it further in this paper.

Individuals eligible for HAP are those who are qualified for social housing support by their local authority, and therefore eligible to go on local authority waiting lists. Individuals in receipt of the HAP will source property through the private rental market, in the normal way. A key initial challenge is finding a landlord who is willing to rent to a HAP recipient. In part this appears to be influenced by a sense that the HAP adds an extra layer of red tape from the perspective of a landlord, as well as some landlords appearing to perceive HAP recipients as higher-risk tenants than those who do not need HAP support. The property is rented directly to the individual tenant (rather than to the local authority), but the monthly rent is paid by the local authority to the landlord.

There are limits to the level of rent that can be paid under the HAP scheme, based on a combination of the property location and the number of people renting. We understand that, in some circumstances, the rent paid by the local authority can exceed the defined limit by up to 20%, while in extreme cases higher rents can be financed by HAP on a case-by-case basis. In addition, there is some capacity for the tenant to pay an additional 'top-up' rent, if the local authority is satisfied that this is affordable. We understand that the local authority, in determining whether a top-up rent is affordable, applies a broad rule of thumb that rental payments in aggregate should not exceed 30% of net income.

The combination of these factors means that the level of rent that can be earned on properties rented to HAP recipients should not be materially below market rent levels. Therefore, while renting to HAP recipients could impact the level of rent that can be achieved, the return to investors should not typically be materially reduced relative to a commercial property fund.

To facilitate payment of the rent by the local authority, the individual tenant pays a portion of the rent directly to the local authority (with the level of rent paid by the tenant to the local authority determined based on household income levels). Considerable further information on the operation of the HAP programme is available at its website.⁴

3. Pooled investment funds

Pooled investment funds can take various legal forms, and have been a commonly used investment structure for Irish and international investors over the last number of decades. Most investment business that takes place through Irish insurance companies (whether this is people investing lump sums, or pensions-related savings) has accessed the stock markets and other potential investments through unit-linked funds. Unit-linked funds are funds offered by insurance companies that allow investors to pool resources and access investments that may not otherwise be easily available to them individually. In addition, there is a wide range of pooled investments such as mutual funds and Undertakings for the Collective Investment in Transferable Securities (UCITS) which investors can access directly—typically through stockbroker accounts or online trading platforms.

⁴ See <http://www.hap.ie/>.

At end 2018, information returns for a sample of the largest life insurance companies in Ireland (excluding Irish companies selling in other European territories) showed total unit-linked assets under management of about €75 billion.⁵ This excludes unit-linked assets held by non-Irish insurers in respect of Irish policyholders, and does not include pooled investment fund assets held by Irish individuals outside insurance structures, e.g., through mutual funds or real estate investment trusts (REITs).

The key advantages of pooled investment funds are broadly as follows:

- Some assets are only available in unit sizes that are too large for most individual investors to acquire. For example, an Irish investor wishing to access the commercial property market would not typically have the option of purchasing a commercial building to rent to companies. However, a commercial property fund would allow an investor, often with relatively modest amounts to invest, to buy units in a fund which in turn invests in commercial properties. In effect, this is equivalent to a large number of individuals pooling resources to purchase commercial properties, with each individual effectively owning a small portion of each asset held (and hence benefiting from a small portion of rental income, sale proceeds etc., net of any costs).
- Even where assets are available in unit sizes that an individual investor could access, there can be benefits of accessing them through a pooled fund structure. For example, an individual wishing to invest in shares in European companies could do so by buying shares directly. However, to gain a suitable level of diversification, the individual would need to acquire shares in many companies. Either the individual would need significant resources to achieve this, or the deal sizes for each individual company purchased would be quite small, leading to disproportionate levels of cost. Joining forces with other investors through a pooled fund increases the overall level of resource and allows greater diversification and better economies of scale.
- Similarly, running a balanced investment portfolio can require considerable expertise. For many investors this would be a risky and time-consuming exercise, and many therefore look to delegate this activity to a professional investment manager. Pooled investment funds are a natural fit for investors who want to access stock market and other asset class returns without making ongoing (weekly or daily) investment decisions.

Each of these advantages of pooled investment funds could point towards the possible ability of this form of investment to meet the challenges of financing social and affordable housing. In particular, while individuals may not feel empowered to tackle a crisis of this magnitude, and will not feel that they can make a meaningful contribution to solving the crisis themselves, there is certainly potential for the purchasing power of many individuals to act collectively towards a common goal. Pooling resources through an investment fund could facilitate financing the development or acquisition of rental properties, while the fund governance could ensure that the properties were rented to the target audience, at affordable rates. In addition, the skill set required to build a property portfolio of this nature, along with the purchasing power needed to generate cost efficiencies through economies of scale, means that a large pooled fund could be ideally placed to do this most effectively. Expertise could be centralised and managed efficiently, while strong governance arrangements, coupled with clear communication, could give full transparency around operational efficiency and cost for investors.

The concept of pooled funds we are presenting differs from these options by focusing entirely on social and affordable housing, and by facilitating direct investment from members of the public, pooling individual investment amounts, which may be relatively modest, into a larger collective fund.

A key issue in making this concept work effectively would be determining the legal structure of the fund. Ideally the fund structure would:

- Be legally secure
- Facilitate open and transparent governance
- Be tax-efficient
- Facilitate individual (retail) investors as well as institutional investors and pension funds
- Allow investment from outside Ireland
- Facilitate long-term, patient investment in illiquid underlying investments (i.e., properties)

⁵ Source: Milliman research based on Solvency and Financial Condition Reports for end 2018 published online by a sample of five domestic Irish life insurance companies.

SIDEBAR: EXAMPLES OF SOCIAL HOUSING ENTITIES

Urbeo and Clúid are examples of organisations active in this area, though we understand that neither is open to direct investment from the public.

Urbeo is an example of an investment platform heavily investing in Dublin housing. The fund combines investment from a US firm, Starwood Capital, the Irish Strategic Investment Fund and other investors to build a portfolio of Irish residential rental property. Notably, the platform has a strong social and affordable housing element. We understand that about 20% of the rental properties in the portfolio are rented to tenants supported by the HAP scheme, while about 10% of the properties are rented to the state for social housing purposes. The fund partners with developers, builders and housing associates.

Clúid is a nonprofit charity providing over 6,500 homes in Ireland to people in need. Clúid aims to maximise business success as a housing association and then reinvest all profits made. Clúid carries out its housing objectives in various forms, including building, buying and leasing. All of Clúid's housing is occupied by households with support from local authorities. Tenants availing of Clúid's housing are, for example, in receipt of the HAP scheme. As Clúid is a well-established charity with the aim of helping those in social housing, it gives its tenants greater comfort that their tenancy is seen as more long-term.

We understand that a number of options are available. Partnering with a life insurance company to create a new internal unit-linked fund of the insurance company would be one possible approach. While this approach would address a number of the requirements listed above, it would potentially limit the target group of investors for the fund.

We believe that a more advantageous approach would be to set up a real estate investment trust (REIT). A REIT is a publicly listed company whose main activity is the ownership and management of property-related assets. REITs allow investors to hold property investments through shares, making them a tax-efficient option.

REITs can be set up as open-ended or closed-ended. We have focused in this discussion paper on a closed-ended REIT as we believe this structure would be better suited to the objectives of the fund. The main benefit of a closed-ended REIT, when compared to a unit-linked pooled property investment, or an open-ended REIT, is stability in terms of the underlying asset portfolio. With unit-linked funds and open-ended REITs, there may be times where requests for the redemption of investments exceed the level of cash within the fund. In these circumstances, properties would need to be sold to facilitate the redemption. This can be a time-consuming process, leaving investors locked in to their investments at a time when property prices could be in decline, or forcing a sale of assets which could be detrimental to underlying renters. In contrast, investors in a closed-ended REIT can redeem their investments by selling their shares in the REIT, which would not impact directly on the investments within the REIT itself. Of course, closed-ended REITs are exposed to stock market volatility in the same way as other equity investments and investors may face liquidity challenges if there is insufficient demand for the shares of the REIT.

Another advantage of REITs is that the value of the investment is determined by the share price in the market. By contrast, unit-linked investments require a regular valuation of unit prices based on the value of the underlying assets, net of management fees.

REITs do have some drawbacks, particularly in relation to the criteria that must be satisfied for a company to be classed as a REIT. They include requirements for the majority of the investment to be in property (75%), restrictions on gearing (less than or equal to 50%) and requirements for a large proportion of rental income to be distributed as dividends (greater than or equal to 85%). In addition, while the minimum number of properties that a REIT must hold is quite low,⁶ the management costs associated with running a REIT (e.g., salaries, directors' fees, audit fees, head office costs etc.) are likely to be reasonably high (possibly in the region of €2 million to €3 million⁷). Therefore, a REIT would need to operate at a reasonable size to allow for a sufficient economy of scale in terms of covering these costs.

⁶ At least three properties are to be held in the portfolio within three years of listing, and no one property can be greater than or equal to 40% of the overall portfolio.

⁷ This is based on the 'General and administrative expenses' reported by another residential property REIT IRES in its annual reports for the period 2014 to 2017. The 'General and administrative expenses' for IRES's REIT's from 2 July 2013 (date of incorporation) to 31 December 2014 were €2.2 million. Therefore, €2 million is likely in the region of the minimum level of expenses incurred in operating such a company.

SIDEBAR: THE FINANCIAL SERVICES INDUSTRY AND AFFORDABLE HOUSING

The involvement of the financial services industry in the financing of social and affordable housing is not a new concept. Apart from Irish entities like Urbeo, there are a number of international financial services companies active in this space.

In the UK for example, many insurers are directly involved in financing social housing programs. Typically, this is achieved through debt financing – i.e. the insurer provides loans to housing agencies to finance the provision of affordable housing. For example, Pensions Insurance Corporation (www.pensioncorporation.com) details a range of debt financing transactions for housing agencies, such as the provision of £100 million of debt financing to the East Midlands Housing Group in July 2019. Legal & General (L&G) is another active in this sector. As well as providing debt financing for affordable housing, L&G also invests directly in affordable property assets, such as the £44.6 million partnership with Croydon Council announced in April 2019.

For the majority of UK companies, the assets (whether loans or direct property investment) are held directly by the insurer (typically used to “back” annuity liabilities). This contrasts to our proposed pooled investment fund which would allow individuals to invest directly in the provision of social and affordable housing.

In the US, REITs focused on affordable housing (generally referred to as low and middle income housing) are common. Structures vary considerably, but often involve debt financing of low and middle income housing providers. We believe the rules for attaining REIT status in Ireland are likely to limit the extent to which an Irish REIT could hold assets other than direct property assets, and this may prohibit an Irish REIT from providing loans to housing agencies. However, the presence of commercial US REITs focused on financing low and middle income housing evidences a potential role for the financial services industry in this sector.

A REIT structure could facilitate both individual and institutional investors, and would be accessible to non-Irish investors. Insurance companies keen to access the residential rental market, or to contribute in a meaningful way to alleviating the social and affordable housing crisis, could for example invest a proportion of their internal property funds in the REIT. It is difficult to access current statistics on the total level of property investment within internal-linked funds of Irish insurers, but based on older returns provided by insurers to the Central Bank of Ireland we conservatively estimate that this is in excess of €3.5 billion. On this basis, an allocation of, for example, 5% of internal property funds to a REIT focused on social and affordable housing would provide an initial fund of about €175 million as well as providing insurers with a means to access residential rental property.

There may be other investment structures that could achieve similar outcomes. For example, an Irish Collective Asset-management Vehicle (ICAV) could be an option for this type of pooled investment structure though it may bring infrastructure challenges in terms of calculating ICAV prices on a regular basis (which could result in higher ongoing operational costs relative to a REIT where prices are set by the market).

OPPORTUNITY FOR COLLABORATION

At this point, further research is required to determine the most advantageous legal structure for an investment fund of this nature. Our initial assessment points to a REIT as the most opportune approach. Given the ambition of this project to tackle social and affordable housing, we would welcome the considered views of any legal firms with relevant experience in this area who might have deeper specific expertise here than our own.

- Is a REIT structure the best way to proceed, and if so is a closed-ended REIT the optimal approach?
- What are the key challenges that would need to be addressed to establish a REIT and operate it on an ongoing basis?
- Is it possible for a REIT to finance social and affordable housing by providing loans to housing agencies?
- Should other structures like ICAVs be considered?
- Would internal-linked funds of insurers consider investing in an asset like this and what are the implications of this for governance, use of gearing etc.?

4. Operational challenges

Typically, a pooled investment fund that focuses on property investment will need to address a range of operational challenges, including:

- Legal structure and obligations
- Sourcing properties
- Sourcing and managing funding
- Integrating to existing structures such as the HAP and local authority social housing activity
- Furnishing properties
- Identifying tenants
- Ongoing property maintenance
- Financial reporting and regulation
- Investor reporting and relations

There is a balance to be struck between how much of this activity is carried out directly by the fund through in-house expertise, and how much is outsourced. Initially, at least, the most efficient way to address these challenges is likely to engage external expertise in the relevant areas. As the scale of the fund grows, it may make sense to internalise more activity.

Given the nature of the fund and its objectives there may be an opportunity to take an innovative approach to some of the operational challenges. Given the corporate social responsibility programmes in place in many leading financial services and professional services companies, it may be possible to develop a collaborative approach that enables a more cost-effective delivery of service.

In relation to identifying tenants, we believe there is an opportunity to develop a user-friendly interface or app that would facilitate matching tenants and families to the most appropriate accommodation for their needs, which could improve tenant experience and also result in lower turnover rates over time.

OPPORTUNITY FOR COLLABORATION

It would be helpful to engage with other professionals who can provide further insights into these challenges. In particular we would welcome the insights of:

- Property management firms with innovative ideas for meeting the ongoing challenges of running a residential property fund of this nature
- Property developers with an ambition to collaborate in providing social and affordable housing solutions
- Legal firms that are keen to use their skills to tackle the social and affordable housing crisis
- Urban planners who could provide useful insights to ensuring that social and affordable housing solutions are implemented correctly
- Software developers with insights into developing an app to match tenants and their properties.

5. An investor's perspective

A pooled fund with a focus on social and affordable housing would offer individual investors an opportunity to join forces with other investors to make a material difference collectively to the homelessness crisis. The key points differentiating this initiative from other options currently available are as follows:

- It's an investment rather than a charitable donation. This may allow people to contribute more as they will be investing in property and it could form a part of an individual's investment portfolio. With the right tax treatment, it may be possible to access the pooled investment through a pension fund, further increasing the potential attractiveness of the investment to individuals.
- The investment will be focused entirely on social and affordable housing, and in particular on helping families experiencing homelessness. We envisage that the fund would provide clear updates on its activities in this area to keep all investors informed of success against targets. This will be a unique opportunity to target investment funds towards tackling homelessness.
- While there are a number of logistics to address, we envisage that the fund would facilitate relatively modest investment sizes (e.g., investments of less than €5,000 should be possible). By pooling many smaller investments together, the fund will have the capacity to buy or develop properties that individual investors could not access.

A key component of the fund is that the governance and communication will need to be crystal clear. The focus of the fund is to deliver returns to investors while also tackling homelessness. Therefore it will be important to manage and contain costs appropriately. This can be achieved through building economies of scale and through developing efficient processes. However, a key component of success will be open and transparent communication with investors along with the strongest standards of corporate governance. We envisage that the fund would be run by a management team overseen by a board. The board would have overall responsibility for setting strategy and the management team would be charged with delivering the strategy. The board would include a majority of independent nonexecutive directors and would adhere to the highest standards of corporate governance.

Investors would have the assurance that their money was being invested appropriately and decisions were being taken based on sound rationales and objective criteria.

If the pooled investment follows a REIT structure, individuals would effectively be purchasing shares in a company. The share price would fluctuate based on supply and demand, though it is likely that the movement in the share price would be heavily influenced by the underlying net asset value of the property portfolio. The investment should therefore behave like a property investment. It will be important to note the risks attached to investments of this nature, which, along with the market risk, liquidity risk and expense risk referred to in Section 2 above, include:

- Legislative risk: There is a risk that changes in legislation will affect the nature of the investment (e.g., tax status, changes to legislation in relation to social and affordable housing etc.).
- Risks associated specifically with the fund could include the fact that focusing on social and affordable housing may result in lower returns than could be achieved by a less constrained investment strategy.
- Borrowing (often referred to as gearing), if the fund uses it, can have benefits in terms of increasing the capacity of the fund to purchase properties, but can create additional risks such as increased volatility of performance, increasing the risk of negative returns.

The potential returns for investors will be affected heavily by property market conditions. Prime residential property yields are currently about 4% per annum. As the focus of the fund will not be prime locations, we would expect a yield pick-up of about 1.0% to 1.5% per annum.⁸ However, costs will reduce yields somewhat. On the assumption that the fund reaches a decent level of scale, this could be of the order of 1% per annum, but may be higher, particularly in the earlier years. The focus on affordable rents may also reduce available yields somewhat. Additional yield can be generated over time through rent increases (though the nature of the investment means that there will be some constraints on the level of rent increases that can reasonably be expected in the short to medium term) and through the impact of gearing. Broadly, therefore, we believe it is possible for the fund to provide an attractive potential return to investors, albeit one that is not risk-free. Strong governance and risk management processes will therefore be important.

OPPORTUNITY FOR COLLABORATION

Figures in this section are high-level estimates in an attempt to understand whether the economics of the fund might stack up, and not intended to be predictors of expected future performance. We would welcome insights from those active in running or advising property funds of this nature.

- What are the potential returns that can be expected for an investment fund of this nature?
- Are there material additional risks that need to be considered?
- What are the most appropriate governance structures for an initiative like this?

6. A renter's perspective

Based on our initial discussions with people active in housing charities in Dublin, at present the social housing programme in Dublin is seen by many of its dependents as slow, limited and flawed. Tenants' priorities are affordability, location, quality and certainty, including security of tenure. Given the limited availability of permanent social housing and extensive waiting lists, the government presents the HAP scheme as a subsidised alternative to avoid more temporary alternatives (such as hostels, hotels, shelters and B&Bs—which

⁸ Note that we are not property investment experts. The figures in this section reflect our understanding based on initial conversations with professionals active in this area, but should only be regarded as illustrative.

currently house 1,700 families⁹). This, however, has a number of pitfalls from a renter's viewpoint. Under current legislation, once housed by the HAP scheme the renter is removed from the waiting lists of all housing areas on which they are currently pending. The renter could have been on these waiting lists for many years—they are therefore understandably very reluctant to use the HAP scheme in many cases as they fear that the accommodation arising through the HAP scheme may be more temporary in nature and could remove the possibility of more permanent accommodation arising from their places on the lists.

According to a number of those active in housing charities in Dublin, the primary source of the negative connotations associated with the HAP scheme is the imbalance of rights between tenant and proprietor, which leave tenants with less certainty about the longevity of tenancy. In a situation where private market rental has left a HAP scheme user with an inability to continue a tenancy at the end of a one-year lease (whether through affordability or the property becoming unavailable), the tenant has only been housed for a short period and has forfeited positions on social housing waiting lists. Most rental properties are available with leases of 12 months. For HAP tenants, there is a risk that rising market rents over time may push the rent level required beyond the limits paid by the HAP scheme. This can require HAP users to pay top-up rents if they are to remain in the same property, and for some it may become unaffordable. While the local authority will fund rent increases up to the HAP limits, and in many cases beyond the HAP limits, there are inevitably situations where the out-of-pocket rental expense for a HAP tenant (either through the contribution they make to the local authority or any top-up rent required) creates significant affordability challenges.

A framework that counteracts these issues is essential in order to meet the fund's social objectives. By meeting these needs, the fund is also much more likely to see steady income as it will limit void risk (the risk of properties being vacant between tenancies, and therefore not generating rental income). An ideal place to start would be in areas where the waiting lists are longer, for example areas in the northeast of the city such as Artane, Coolock, Killester and Raheny. The biggest demand is currently for one-bedroom and two-bedroom accommodation. If families are to be a target of the scheme, some essential criteria for people waiting on social housing are proximity to schools and ease of travel to the city centre. It has also been shown that families are reluctant to move into areas that are seen to be solely or largely comprised of social housing in one particular complex or area. HAP users, who may be paying any rent increases out of their own limited incomes, would also welcome a certain level of rent price guarantee.

From discussion with various organisations, it seems HAP users are somewhat more comfortable renting from an institution rather than an individual. There is a risk with single landlords that circumstances may change and tenants will be asked to leave (for example, if the landlord needs to sell the property or chooses to discontinue renting it). While an institutional landlord may also face changed circumstances which could lead to sales of property, for example, an institutional landlord is likely to provide a more stable, long-term rental agreement. It may also be possible to explore leasing structures that would help provide tenants with greater security of tenure, for example setting out terms within which guaranteed renewability of leases could apply, or providing leases that extend beyond one year.

7. Other challenges: Unintended consequences

There are certain logistical issues to be aware of to ensure the continued viability and success of such a fund, both from an investment and social standpoint. Some of these are stated in Section 4 of this report above. There are also some secondary issues which should be accounted for.

Given the nature of the investment and its intended market, the fund needs to strike an appropriate balance between its social objectives and the fact that it is an investment fund with obligations to its investors. It should be run with full transparency to ensure that investors and tenants understand the philosophy and approach of the fund clearly, and will not be surprised by the approach taken.

Ideally, the fund would express at the outset the percentage of residential properties it intends to designate to HAP scheme users and the percentage allocated to other social housing users. While some flexibility will be required as circumstances develop, the activity of the fund should be consistent with the principles set out, and it should also strive to have clear legal literature in place with regards to tenants' rental longevity rights and any specific rent price guarantees it offers, should it wish to do so. It is likely unavoidable that issues will arise with a small minority of residents (as with any large rental properties). This might be in relation to timeliness of payment,

⁹ Homelessness Report, May 2019, op cit.

behaviour, noise, general property upkeep etc. It is important that the fund has a clearly defined approach for addressing such issues if and when they arise. A management company is likely to have experience in dealing with such situations. Working with a well-established management firm and monitoring its approach to controlling these issues will help to manage these risks.

Social housing also carries a certain stigma in Dublin. It is quite possible that in purchasing or building properties in certain areas and making a public statement that they are intended to be used, at least partially, for social housing could provoke objections, complaints or other forms of resistance from residents of the respective areas. This is likely to be exacerbated if the fund chooses to geographically concentrate its purchases to pursue economies of scale. Past cases similar to these have seen longstanding residents of the areas particularly aggrieved, as they believed the development's intentions were not expressed to them and they felt deceived. To mitigate these issues, it is essential that residents of the area feel reassured—for example by informing them that the fund has a clear framework in place for tackling antisocial behaviour should it arise, as well as highlighting the role of Garda vetting in social housing applications and the application process for HAP support, which considers convictions under a number of public statutes including antisocial behaviour and public order offences.

It is also important to note that the fund proposes to have a mix of both social housing (rented directly to the local authority) and affordable housing (rented through the private market to tenants in receipt of HAP support). Striking the most appropriate proportion between the two could minimise the perceived risk of antisocial behaviour and resistance from local residents. Managing this risk may also entail a trade-off between concentrating residencies for ease of management, availability and value for money and spreading out the investments to ensure their long-term sustainability, attractiveness and avoidance of perceptions of excessive antisocial behaviour and complaints.

It is possible that a fund of this nature could have a distorting impact on the rental market, especially if properties are rented at below market rates. A further unintended consequence of a fund of this nature is that it could compete with first-time buyers struggling to find housing within a price range, making it harder for them to find suitably priced homes. The concept of a 'cuckoo fund' has received considerable coverage in recent months and it is possible that this fund could be regarded as such. In other words, it could be viewed that the fund would reduce available properties and therefore further hinder first-time buyers who already face ever-reducing access to housing within their price ranges.

It is also possible that the fund would be seen as further competition for residential property and therefore as increasing the cost of housing for charities trying to tackle homelessness. This may be exacerbated as the fund and housing charities are likely to be bidding on the same or similar types of properties. Of course, this would be counterproductive and the fund should therefore have open communication with these charities (to the extent that it is appropriate) in order to coordinate each party's efforts to maximise outcomes.

One potential solution to both of these issues is for the fund to build houses rather than purchase. However, this will have a significant impact on the nature of the funds and the risks to investors. We envisage that the activity of the fund could be a mix between acquisition and development, with a heavier focus on acquisition initially.

OPPORTUNITY FOR COLLABORATION

It would be helpful to understand more fully the potential unintended consequences for charities and others active in this space, as well as for first-time buyers, from a solution of this nature. Understanding, and eliminating or minimising, the impact of such consequences would ideally require engagement with other professions and we would welcome insights from charities active in this space as well as economists and others with relevant experience.

To the extent that developing new properties could help address some of these unintended consequences, it would be helpful to hear the insights of property developers and property fund managers of the implications of adding a greater focus on new builds to the fund.

8. Conclusion and next steps

In the context of the homelessness crisis, the financial services industry is typically seen as playing a negative role. In particular there is a perception of vulture funds buying up underperforming loan books at cheap prices and carefully maximising returns at the expense of tenants or homeowners, and cuckoo funds elbowing first-time buyers out of the housing market.

We believe there is an opportunity for a new type of fund, with a very clear focus on pooling the contributions of individual investors to protect the most vulnerable. Building a fund of this nature will require drawing on a range of expertise across a number of sectors, and will therefore require a collaborative effort. The purpose of this paper is to set out our initial thinking and to invite potential partners to engage with the challenges identified, challenge the approach outlined, and help build a fund that can begin to tackle the Irish social and affordable housing crisis.

If you have any views on the ideas discussed in this paper, please feel free to contact us, using the email addresses on page 15.

9. References and further reading

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