NEF Defined Income Scheme:

Building more Rented Homes

Presentation to Highbury group on housing delivery

10.11.14

What is it?

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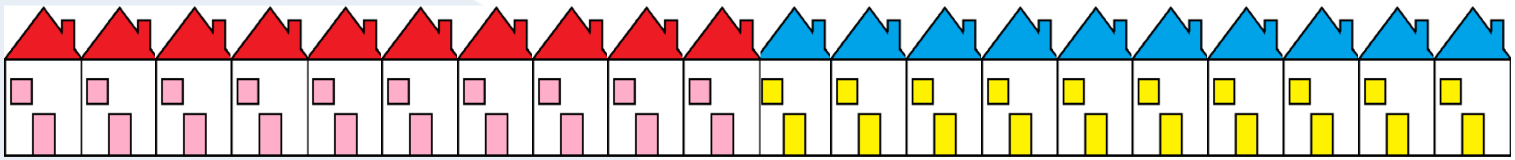
- The NEF Defined Income scheme is a new form of contract between the Local Authority and an RP
- Instead of specifying a number of subsidised units in a scheme, it specifies a maximum income from the units (the “defined income”)
- The defined income comes from a mix of market and subsidised rent units, and should be a more stable revenue flow for the RP, reducing risk
- A key difference at the local authority level is that planning permission allows units to flex tenure between subsidised housing and market rent.
- It can be used on whole schemes or S106

Starting with the Flex Scheme



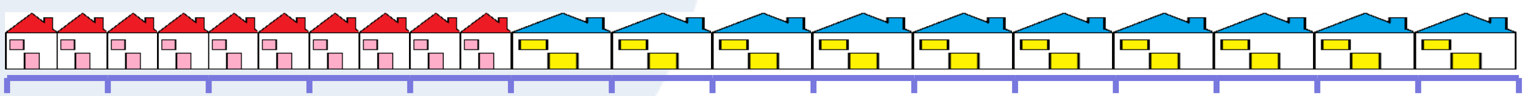
10 subsidised

10 market rent

Financial contribution per house

10 subsidised
£50/week

10 market rent
£100/week



£ 0

500

1000

£1500

£ 1500 / week: this is the Defined Income

It will rise with RPI

Excess Income

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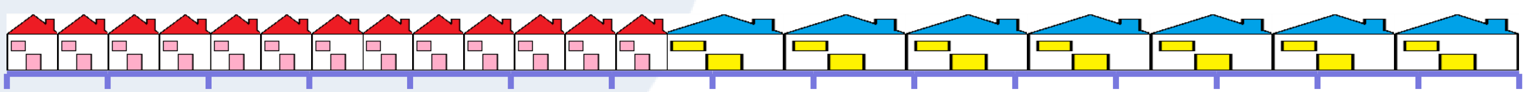
Market rents go up 20%.
This generates extra money to subsidise more units

13 subsidised
£50/week

7 market rent
£120/week

These 3 units were converted



£ 0 **500** **1000** **£1500**

income of £ 1500 / week

This is the Defined Income

Revenue Shortfall

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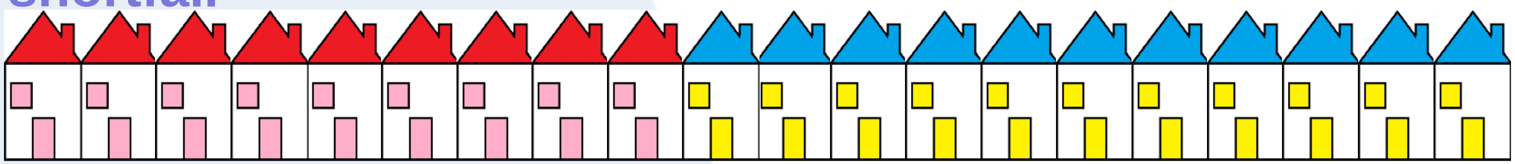
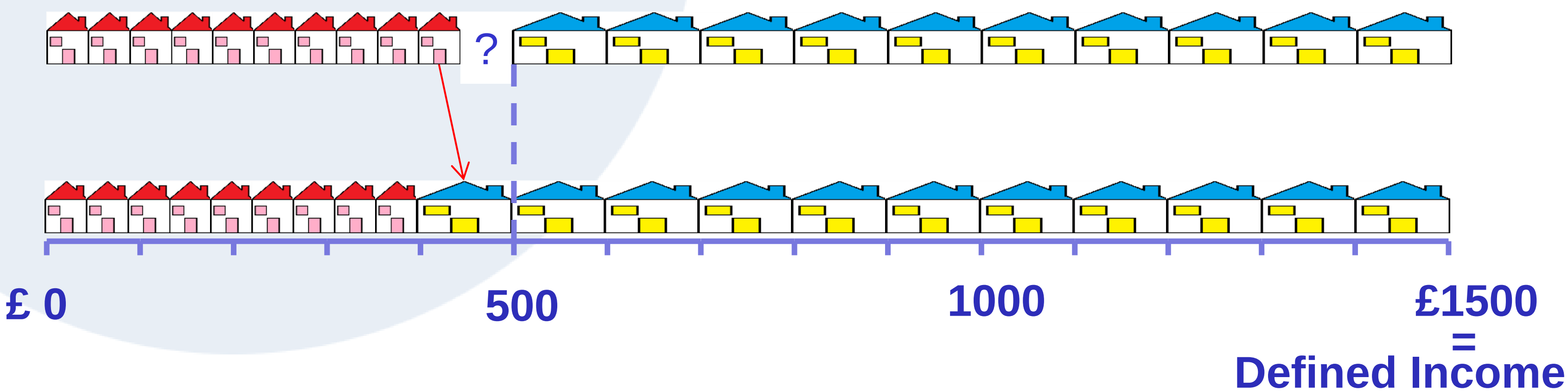
In this example, every subsidised unit doesn't pay £5 in rent, but it could be any reason. This means that a subsidised unit is converted to market rent to make up the shortfall



9 subsidised
£45/week

11 market rent
£100/week



Income Risk Reduction

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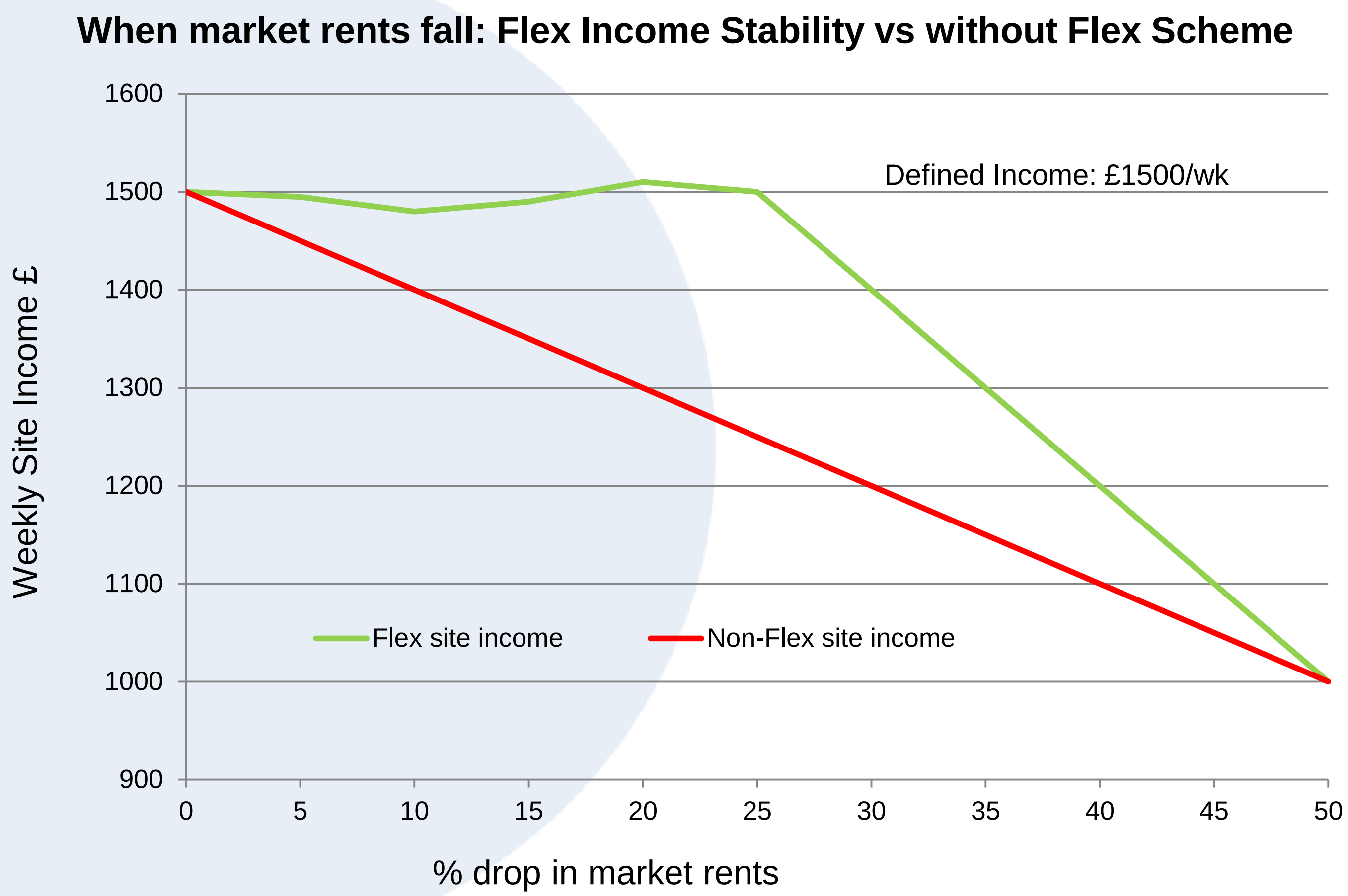


Concepts behind the scheme

- More stable income streams are worth more.
- For this reason, a scheme with a Flex contract on it will generate more value.
- This excess value can be used in several ways:

➢ Either to subsidise more housing *(inherent additionality)*

➢ Or to pay more for the land *(site additionality)*

➢ Or a combination of the two

- In addition, an income stream rising with RPI has strong financial benefits *(financial additionality)*

Types of Additionality

We have identified 4 basic types of additionality

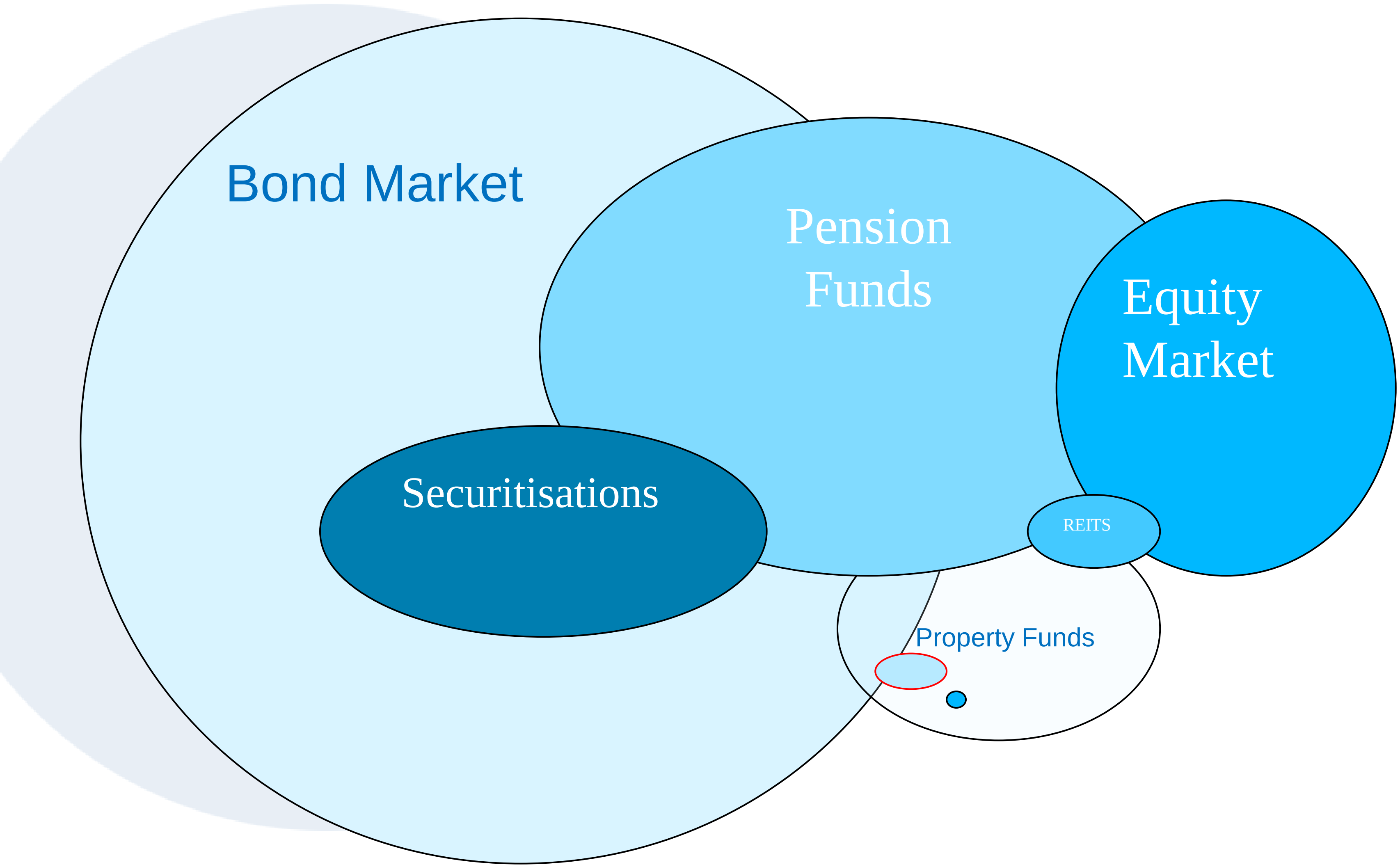
- *Inherent additionality* – the direct effect in housing terms of putting the scheme on a particular site.
- *Site additionality* – sites that would not otherwise have come forward that can, if the Flex scheme is used, due to capacity for increased payments
- *Financial additionality* – improvements in access to index linked finance and capital recycling.
- *Social additionality* – benefits of increased supply, mixed communities, & better quality private rented housing

Orbit: A case study

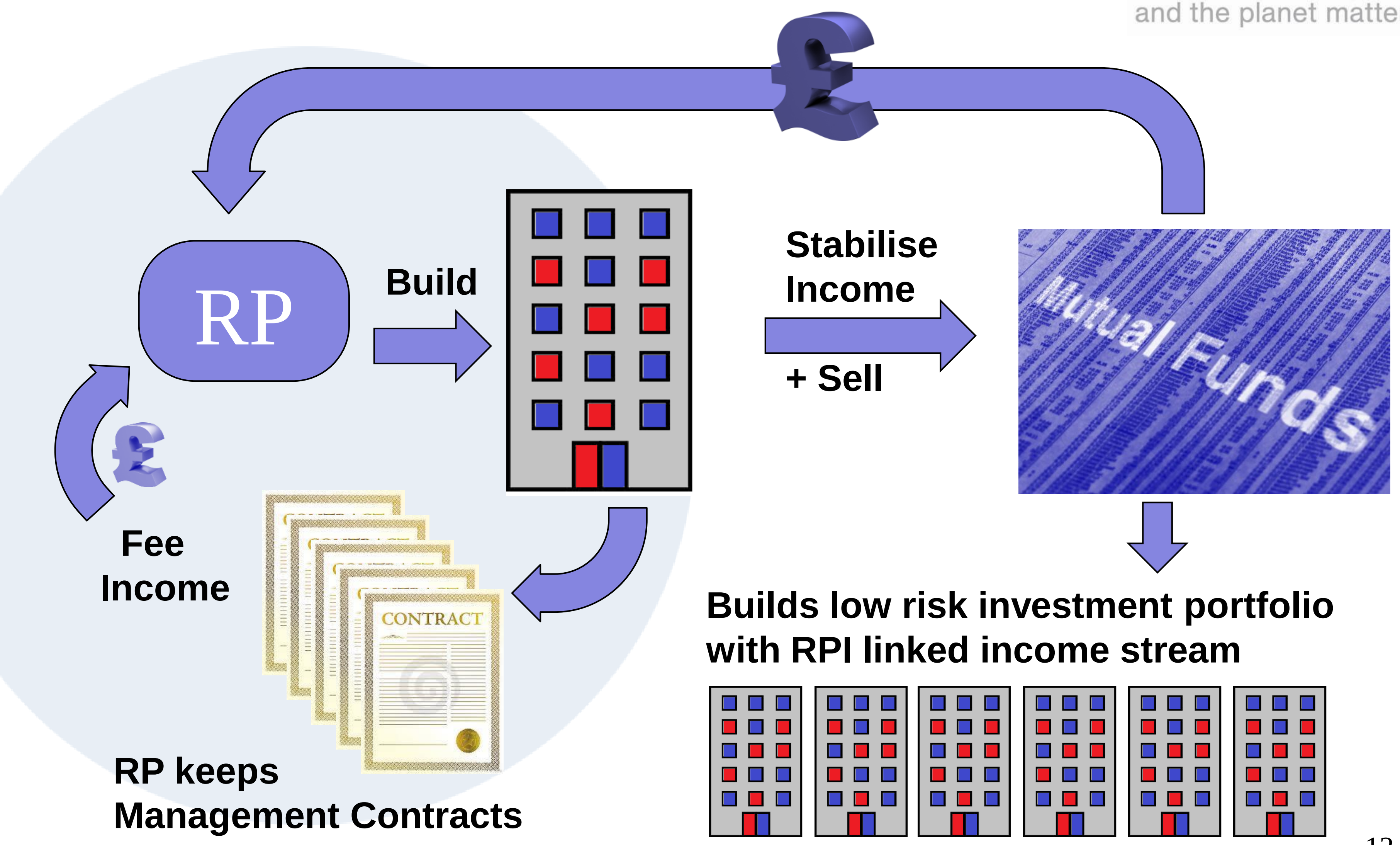
- Orbit are targetting building 12,500 homes by 2020
- They are only currently able to finance 9,500 of these using current headroom
- Non-recourse funding like this in an SPV would enable them to access funds to fund the remaining 3,000 homes using cheaper index linked funding
- Potential access into new funds e.g. equity markets via REITS and non-specialist property funds

Pots of Money?

In the broader context – Asset Allocation



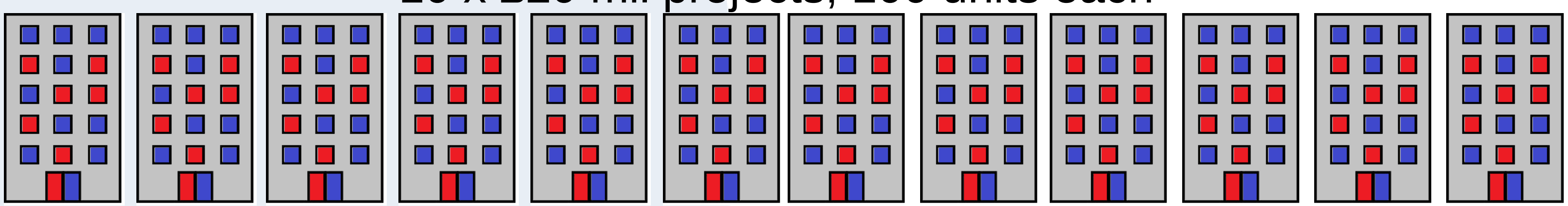
Capital Recycling



Start with some cash

£ 200 million

10 x £20 mil projects, 100 units each



400 social and 600 market rent units

(assuming 40% social)

~The money is lent for 10 years~

The Flex Scheme Refinances

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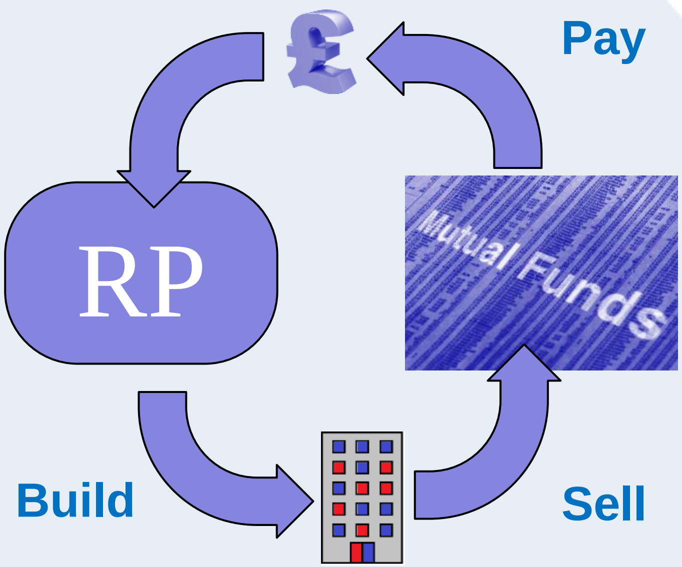
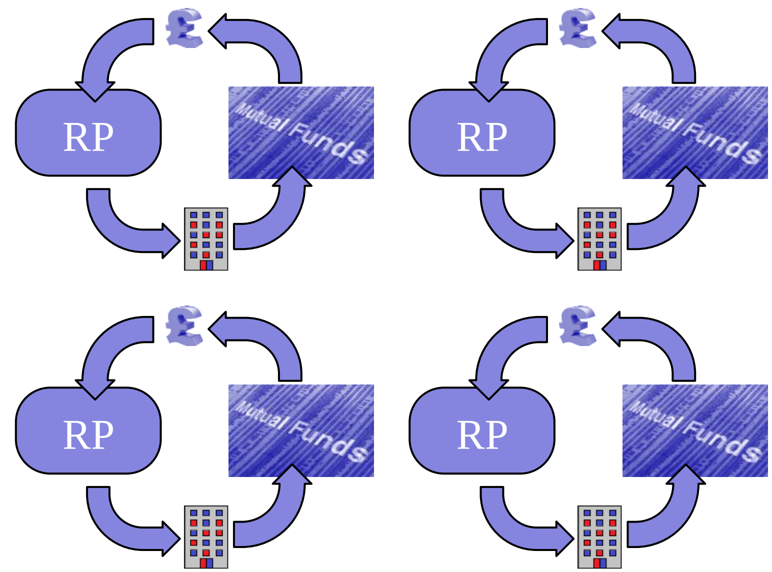
Every 2.5 years



In 10 years



Impact of capital recycling

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£ 200 million

1 loan for 10 years

OR

4 loans for 2 ½ years

400 social

600 market rent units

(1,000 units in total)

1600 social

2400 market rent units

(4,000 units in total)

WHAT if we lose social Housing?

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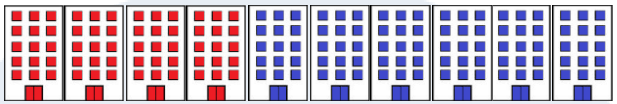
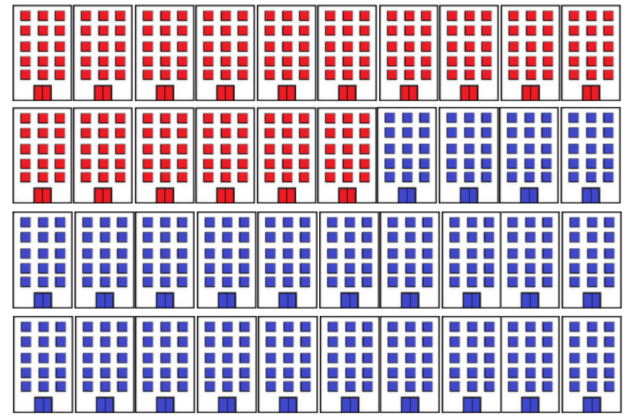


400 social

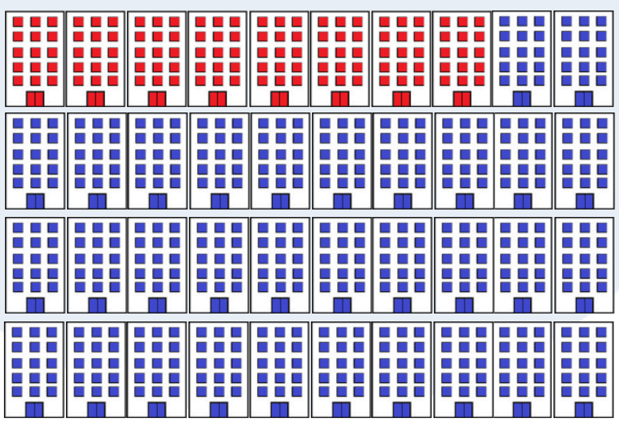
600 market rent units

OR



1600 social

2400 market rent



800 social

3200 market rent

(institutionally managed)

Disaster! HALF social housing is lost!*

* e.g. through a fall in market rents