Tirion Group

Tirion Group Ltd
Tirion Homes Ltd
Tirion Investments Ltd
Ely Bridge Development Company Ltd
Parc Eirin Development Company Ltd
Whiteheads Development Company Ltd

SHS 08
Ymgynghoriad ar y cyflenwad o dai cymdeithasol
Consultation on social housing supply
Ymateb gan: Tirion Homes
Response from: Tirion Homes

Senedd Committee on Social Housing Supply 2024
Written Evidence, April 2024
David Ward, CEO, Tirion Homes,

1.0 Tirion Background

1.1 Tirion is a not-for-profit Community Benefit Society formed by Welsh Government and Principality Building Society in 2012. Tirion was created to provide a vehicle to deliver large regeneration projects with a focus on affordable housing and using Institutional investment negating the need for Social Housing Grant. Tirion will complete:

- The Mill in Cardiff this summer which provides 845 mixed tenure homes 448 of which will be affordable including 124 Social Rent properties;
- Royal Victoria Court in Newport in Q1 2025 for 536 mixed tenure homes 268 of which will be affordable; and
- Parc Eirin in Tonyrefail in 2026 (phases 1-3 already complete) providing 215 mixed tenure homes, 134 of which will be affordable and include net-zero energy infrastructure.

1.2 Tirion projects are being delivered in collaboration with WG, PBS, M&G Investments Ltd. and RSLs to deliver the best outcomes possible in line with WG policy. Crucially WG has provided loan finance and a guarantee to enable the projects to proceed. The projects will:

- provide mixed tenure housing including social rent;
- be completed without Social Housing Grant;
- offer secure contract tenancies;
- adhere to WG space and performance standards; and
- draw down long-term finance from M&G Investments Ltd which will be used to pay back WG loans.

1.3 The 50-year debt finance from M&G obligates Tirion to deliver the highest standards of tenancy management and planned/reactive maintenance. On retirement of the debt the properties will revert to Tirion, or other partners, to guarantee their affordability status in perpetuity.

2.0 Housing Market Context

2.1 Lack of supply across all tenures has seen both house prices and private rents increase to an extent where affordability is a key issue for a growing proportion of the population particularly where wage growth is not matching property cost increases. This is exacerbating need across all affordable tenures.

2.2 Increases in interest rates over the last 18 months has affected affordability in the first time buyer market and whilst rates have stabilised it is clear we will operate in a higher interest rate environment for the foreseeable future probably returning to historic norms of 3-5%. The IMF has recently forecast that interest rates in the UK will remain at around 4% until 2029. This is pushing more people into a restricted and somewhat overheated rental market which in turn will inevitably increase pressure for more affordable housing. Whilst house prices have decreased in Wales by 3.6% from their peak in late 2022 they are projected to rise by 21.4% over the next 5 years (Savills) meaning an increasing number of people will be forced to consider renting as their only option.

2.3 Historically rental costs in Wales have been well below the 30% affordability threshold (household income spent on rents). However, since the Pandemic new let rents have risen by 36% (Savills).In 2023 new lets rose by 9.5% and all lets by 7% (Zoopla). This is illustrated at The Mill in Cardiff where our discounted market rents were set at 80% of open market in 2020. Despite CPI plus 1% increases in the intervening years some units now have rents just above 60% of the open market demonstrating how quickly rents are rising above inflation. It is clear that private rents are becoming unaffordable for the majority seeking to rent in popular markets such as Cardiff and Newport.

2.4 The interrelationship between all housing sectors is complex. For example, lack of supply of intermediate rent is creating pressure for social rent as those who cannot afford private rent shift directly to social rent waiting lists instead of accessing intermediate rental properties within their affordability spectrum. It is clear that if housing need is to be addressed then WG, RSLs, LAs, Tirion, housebuilders, contractors and private investors need to collaborate to maximise the delivery capacity of the entire housing sector across all tenures.

3.0 Progress towards meeting the target of 20,000 low carbon social homes for rent; and the extent to which current and projected levels of social housebuilding are likely to meet housing need

3.1 5775 units were delivered in the first two years of the WG programme but this included refurbished and properties purchased directly by RSLs from the private sector. Research (Savills) shows that an average of 3600 homes were required from 2019 and this target was only met in 2021 (including all tenures with 2443 being social rent). 2023 was the second best year for delivery but was still 5% short of target. Projections (Savills) for 2024 suggest delivery will fall back further. The trend of RSLs purchasing completed private sector homes with grant improves tenure balance but does not address overall supply.

3.2 Intermediate rent typically accounts for less than 10% of affordable homes being delivered which represents a huge opportunity, not least for securing institutional investment. The lack of supply of intermediate rent creates unnecessary pressure for social rent by creating a significant gap between the private rental market and the social rented sector.

3.3 The impact of inflation, tightening credit markets, slowdown in private housebuilding and lack of capacity in the construction sector means there is little prospect of the 20,000 target being achieved. This is exacerbated by huge pressure on Local Authorities to provide temporary accommodation for homeless individuals and families. Even if the 20,000 target is met it will not be sufficient to meet growing need and the historical backlog in affordable homes delivery.

3.4 Savill's research suggests that if the 3600 annual requirement is projected back to 2011 then there is a likely backlog requirement for an additional 12-14,000 affordable homes. If this is the case then at least 5,000 new affordable homes need to be delivered per annum for the next 10 years. Taking current Acceptable Cost Guidance and the traditional intervention rate of 58% then this would require a Social Housing Grant Programme of around £750m per annum to deliver this level of social rented stock. Even if this level of Welsh Government support was available , a combination of the factors that have hindered progress towards the 20,000 target, combined with the challenges discussed below, means the Welsh Housing Sector does not currently have the ability to deliver against this level of need.

3.5 There is an argument that the 5,000 per annum target is conservative as it does not take full account of the impact of the temporary accommodation crisis facing many Local Authorities.

4.0 The challenges faced by social landlords in increasing supply

4.1 Many delivery challenges are shared by the entire housing sector. These include:

Cost inflation – the construction sector has seen unprecedented cost inflation as a result of a combination of factors including Brexit, the Pandemic and conflict in Ukraine all of which impacted supply chain and labour costs. This is illustrated by inflation of our Parc Eirin Scheme where costs rose 25% between December 2021 and April 2023, severely impacting the viability of the project.

Development / Construction Capacity – There is a lack of availability of resources and skills not just in the Welsh construction sector (which has suffered some notable corporate failures in recent years) but also within organisations promoting projects where project/construction management skills are scarce. Given the size of the Welsh construction sector it is inevitable that construction companies from outside Wales will need to be engaged alongside ongoing support for growing the sector in Wales. Deployment of Modern Methods of Construction (MMC) could assist in capacity but will largely be dependent on the provision of a secure pipeline of orders for the sector. Again there have been several notable UK Corporate failures in the MMC sector in recent years.

Utilities – Securing servicing / adoption agreements with utility providers is a time consuming and expensive process. Furthermore the move towards net-zero relies extensively on National Grid capacity to deal with all-electric solutions for heating and hot water. This capacity is often unavailable without significant reinforcement which may not be affordable and, at best, adds delay / impacts viability. Engagement with energy providers is critical in ensuring capacity is available to support housing growth areas and investment programmes are targeted to areas of highest demand.

Development Constraints that impact viability – Most of Wales operates in marginal markets and development constraints often make projects unviable. Good examples are the impact on net-developable areas of SUDs regulations and phosphate mitigation requirements for schemes in rural locations. Recognition of these factors in national infrastructure investment programmes and the planning process will be increasingly important if we are not to leave communities behind where viability is the key inhibitor to development.

Statutory approvals – Planning remains a major impediment to delivery and, in particular, the pace of delivery (see below). In addition highways and drainage agreements/adoption are also a major factor that exacerbates delay. Inflexibility of statutory providers often adds unnecessary costs to development.

4.2 Challenges more specific to Social Landlords include;

Viability – the tightening credit market and higher interest rates has impacted the viability of new projects and increased the reliance on grant. In addition, RSLs must comply with their debt funders financial covenants which have become more onerous thereby reducing financial capacity. RSLs have significant restrictions on their Balance Sheet exposure which makes it much more difficult for them to deliver major regeneration projects. Indeed this is one of the main reasons WG and PBS created Tirion in the first place. Financial constraints are not going to loosen any time soon which means it is imperative that new sources of finance are secured to accelerate delivery.

WG Standards have undoubtedly guaranteed new homes quality where SHG is used. However, associated increased costs have largely been borne by the SHG programme meaning less homes are being provided per £ spend of SHG. One recent example is a scheme for 48 1bed apartments for social rent which has attracted around £10m of SHG. This emphasises the need to secure more institutional investment so that SHG can target schemes and communities most in need;

Transition to net zero is a significant cost challenge. Part L compliance adds between £7k and £12k costs per unit and reaching net-zero performance adds a further £8-£12k. In most markets in Wales these costs cannot be borne as a construction cost whilst maintaining viability. In the short-medium term other ways of financing these works need to be found, primarily working with infrastructure investors (see 5.8 below);

4.3 Tirion is primarily involved in the delivery of large scale regeneration projects with a focus on affordable housing. Challenges for delivering regeneration projects include;

Finance –Regeneration projects, by their very nature, often require significant upfront investment in site preparation, design and planning. Projects also carry significant construction cost risk due to their length of delivery. As a result the track record of delivering major regeneration projects in Wales has been poor given the widespread availability of large brownfield sites in the post industrialisation era (Tirion schemes being a notable exception). There is a clear role for WG and the public sector in facilitating the delivery of regeneration projects particularly given the appetite of financial institutions to provide long term investment (see below).

Public sector appetite for risk – The reluctance of the public sector to take reasonable risks to facilitate the delivery of major projects is a key inhibitor to delivery (again the Tirion model is a notable exception). Risk is often assessed as an absolute factor rather than a balance between risk impact, likelihood, benefits and disbenefits. A change in attitude to risk will be critical in securing additional private sector/ institutional investment.

Skills and expertise – the relatively poor track record of delivery of major regeneration projects in Wales also means there is a shortage of specialist skills and expertise required to deliver these complex multi-faceted projects.

Tirion is well placed to provide expertise and resource to deliver large scale regeneration projects with a focus on affordable housing being the only organisation operating in Wales currently delivering such projects at The Mill, Parc Eirin and Royal Victoria Court in Newport.

5.0 The opportunities and risks in increasing government borrowing and institutional investment

5.1 WG and Local Authorities are facing severe budgetary constraints, restricting their ability to offer more and continuing grant assistance across the sector. RSLs are strictly regulated and all but the largest organisations struggle to raise enough capital for major projects due to balance sheet restrictions and a significant tightening in the credit markets.

5.2 Published data shows 75% of affordable units are being delivered using grant with low cost home ownership making up a further 10%. 5000 new homes with an average SHG requirement of £150k per unit would require £750m SHG per annum. 75% of the 5000 would require a minimum of £600m SHG per annum. There is a question whether 5000 new homes is enough and whether, in the current market, £150k SHG per unit will suffice. This suggests the actual requirement could be over £1bn per annum.

5.3 In the face of this stark reality the only option for securing sufficient finance to deliver the level of affordable homes needed is to tap into the significant appetite of Institutional Investors for affordable housing. The good news is that appetite is strong and Tirion has had strong interest from a variety of investors in addition to M&G Investments Ltd who are providing finance to Tirion for The Mill, Royal Victoria Court and Parc Eirin. It is our belief that successful engagement with the Capital Markets would minimise any need for additional Government borrowing.

5.4 Ideally, WG could attract a range of investors targeting different sectors of the market e.g. suburban housing, new communities, city centre living etc. Key conditions for attracting institutional investment will include;

- Public Sector commitment most typically the provision of land;
- Scale provided by major regeneration projects - investors typically seek a minimum investment of £100m with £300m+ preferred;
- Committed pipeline of sites to ensure investment can be scaled up;
- Untapped capacity in a segment of the market e.g. intermediate rent;
- Third parties providing/underwriting construction finance – this can be a combination of public and private sector as used in the Tirion model; and
- Experienced delivery organisation with proven track record such as Tirion.

5.5 A good comparable of what can be achieved if the right conditions are put in place is, L&G's £1bn investment programme into central Cardiff. Given the scale of housing need in Wales there is no reason to believe this could not be replicated by one or more investors in the housing sector. In order to achieve this WG needs to develop a range of tools that bring forward major schemes quickly to demonstrate commitment and Wales ability to satisfy investors' appetite. These might include:

- Efficient and transparent procurement;
- CPO to assemble sites;
- Clear pipeline of projects with indicative delivery programmes;
- Identification of organisations (including Tirion) with delivery track record;
- Formation of collaborative partnerships to manage delivery of major sites;
- Planning performance agreements with relevant local authorities;
- Early engagement with utility providers to ensure capacity;
- Loan finance (including FTC) for advance site preparation works;
- Construction cost guarantees;
- Medium term rental guarantees.

5.6 The risks and potential mitigants associated with these tools are:

- Abortive CPO costs if scheme does not proceed means sites need to be carefully selected;
- More than one investor needs to be engaged not just to bring scale be in case one investor pulls out of a funding agreement. Long term risk very low as income generating homes in high demand will be relatively straightforward to refinance;
- Lack of organisations with track record. There will be a need to form strong partnerships where stakeholders can benefit from experienced partners such as Tirion;
- Loan finance will be at risk but debt can be re-structured over a longer term based on rental income if institutional finance is not secured;
- Construction cost guarantees – Risk likely to be restricted to 30% of costs (typical LtV). Risk can be further mitigated through rigorous contract management by an experienced organisation such as Tirion. Consideration should be given to partnering with contractor/developers where construction cost risk can be mitigated / balanced by sales risks/values;
- Medium term rental guarantees (5-10 years) could help accelerate institutional investment. Risk should be low due to high demand for properties and can be further mitigated through the use of liquidity reserves financed through the transaction to deal with void risks.

5.7 The above risks need to be assessed in the context of the likely reduction in the availability of SHG, but also an understanding that a failure to address the housing crisis will result in enormous economic and social costs to Wales in the long-term. Maximising institutional investment in affordable housing in Wales will be low risk with high outcomes. It will not only help reduce potential borrowing to a minimum, it will also enable SHG to be targeted to communities most in need whilst incentivising efficiency and innovation. To successfully facilitate delivery, WG and the Public Sector in Wales will need to develop a more sophisticated approach to risk assessment that considers; macro as well as micro risks; the likelihood of risk materialising; the balance of risk rather than as an absolute/theoretical risk; the balance between risk and benefits; and the implications of the risk materialising and how these could be mitigated.

5.8 One overlooked opportunity to secure institutional investment in social housing is in the area of net-zero energy performance. There are an increasing number of companies/investors offering to provide infrastructure at a reduced or zero cost to developments based on long term models where energy and maintenance savings are used to finance capital costs on a 25-40 year basis. In some models Companies make additional income by acting as the Energy Services Company for the development. Many of these companies are backed by major institutions who recognise the commercial and social value of investing in net-zero infrastructure. These models are mostly predicated on delivering large-scale developments and could be critical in the early adoption of net-zero on major regeneration projects.

6.0 How effectively the planning system is supporting social housebuilding

6.1 Planning Policy across Wales supports the provision of high proportions of affordable housing. However, the primary tool used for determining the actual provision is a viability assessment agreed as part of the S106 process. This tends to deliver much lower proportions of affordable housing than policy would normally dictate due to developers demonstrating impact on viability. Where LPAs insist on a minimum provision, the actual delivery of affordable housing is suppressed as schemes do not proceed on viability grounds.

6.2 The primary issue for major applications is the length of determination which can sometimes take 3-4 years or more until consent is finalised. This impacts on viability and deters developers, including RSLs, from pursuing major schemes. This could also be a significant deterrent to Institutional investors.

6.3 Planning performance agreements could be used to help deliver consents more quickly. Alternatively, planning policy could recognise the value of affordable housing and net-zero energy performance by enshrining presumptions in favour of consent where 50% affordable housing and net-zero energy performance is being delivered on brownfield sites.

7.0 How to improve the strategic management of public and private land for social housebuilding, including compulsory purchase

7.1 The formation of the WG Land Division charged with project development, financing and governance aspects of major projects has been a major step forward. However, it remains the case that Wales has a large number of stalled regeneration sites that show no prospect of delivery in the short-medium term. These sites require a collaborative approach and Tirion's expertise and track record complements existing skills and resources in WG, RSLs and Local authorities. WG should utilise Tirion's skills in developing strategies for delivering large regeneration projects.

7.2 Tirion is an advocate of delivery on a site by site basis within an indicative portfolio likely to be attractive to Institutional investors. This simplifies the governance and legal structures and enables projects to proceed more quickly and in parallel with other projects in the portfolio. Once a strategy has been developed the partners (WG, Tirion, RSL, LA) should look to procure potential contractor/developer partners and specialist service providers (e.g. Energy Service Companies) with the objective of delivering against policy objectives in the most efficient manner possible whilst maintaining control of the land. Flexibility is key as major projects evolve over time as new priorities and funding opportunities emerge. Private housebuilders would be procured as part of the process but control would remain with the partnership.

7.3 As far as major regeneration projects is concerned land availability is not the immediate problem but rather the delivery of projects, many of which are already in public ownership. CPO should be targeted at acquisitions which can add value to major projects by rationalising land, completing land assembly where there is already a major public sector holding and/or improving the performance/viability of projects. CPO should also be considered where major public sector investment improves development opportunities, e.g. South Wales Metro, to ensure the public sector maximises the benefits of its investment.

7.4 Where there are major stalled schemes in private ownership, public partners (including Tirion) should negotiate partnerships to unlock sites. This might include waiving some affordable housing requirement, on the basis it can be privately funded via an investor, in return for the developer providing up front capital for enabling infrastructure.

7.5 A key issue will be procurement. The current default procurement method is for the public sector to enter into some form of Development Agreement with a private developer following a competitive process with obligations to deliver policy compliant objectives. The problem with this approach is that major regeneration projects can take 10 years or more to deliver and by their very nature evolve over time. Development Agreements become increasingly difficult to enforce and control over time and the outcomes become less certain. Tiron believe a much better approach is for control of projects to remain with partnerships between the public and third sectors(Tirion) with elements of the project being competitively procured at the appropriate times. This would be an evolution of the Tirion model with WG, RSLs and LAs taking key roles in the Governance and delivery of major projects.

8.0 The potential for increasing income from land value capture mechanisms to invest in social housing

8.1 There are insufficient values in the vast majority of Wales to make land value capture an effective mechanism for investment in social housing. Where potential land value increases can be expected due to public investment e.g. South Wales Metro, then land purchase / CPO should be used to control delivery of development aligned with WG objectives. A common theme in the Tirion approach is that the control of land is fundamental to delivering preferred outcomes.

9.0 The Welsh construction sector's capacity to build new low-carbon social homes; the potential for acquisitions of existing homes and remodelling of existing buildings

9.1 As discussed above the capacity of the construction sector in Wales is a major issue and reflects the marginality of the Wales market. It is inevitable that construction companies from outside Wales will need to be engaged alongside ongoing support for growing the sector in Wales if we are to meet our objectives. Reinforcing and investing in the skills base of the labour market will continue to be very important particularly in net-zero energy services.

9.2 The key to building new low carbon homes is securing private investment that removes the development cost from projects (see 5.8). This is much easier to do where there is a long-term owner/manager in place, such as Tirion, as we can take a view on the value of the investment over a 25-50 year lifecycle and fund the infrastructure via a standing charge / payback provision with the investor. Tirion is obligated to maintain properties for a minimum 50 year period through its agreement with M&G Investments Ltd.

9.3 The acquisition of vacant homes has a potential role to play. However, the reasons for the vacancy must be fully understood. Where there are large numbers of vacancies in a single location we must be careful not to repeat historic mistakes and many locations will require long-term social and economic regeneration support in addition to housing improvements.

9.4 Remodelling has a potential role to play but can be very expensive and further complicated by lease structures and planning policy. However, Tirion is an advocate of developing a strategy for redundant commercial buildings in our cities potentially working with specialist developers and the institutional funds to provide mixed tenure housing and community facilities in our major conurbations.

10.0 How local communities can be effectively engaged in social housing developments in their areas.

10.1 Tirion has a successful dedicated community engagement strategy at The Mill delivered with our partners Cadwyn. Success has been built on a multi-tenure approach bringing all sections of the community together through effective communication, events and support. The key is providing sufficient resource to implement the strategy both during the construction period and in the long-term.

David Ward
CEO
Tirion Group Ltd

www.tirionhomes.co.uk

Tirion. Homes

The Mill, 2 Dol Elai, Canton, Cardiff CF11 8GJ
T: 01633 649550 **E:** info@tirionhomes.co.uk **W:** www.tirionhomes.co.uk
Registered Office: 7 Neptune Court, Vanguard Way, Cardiff CF24 5PJ