

Giles Thorley
Chief Executive
Development Bank of Wales

16 July 2024

Dear Giles

Local Government and Housing Committee: inquiry into social housing supply

As you will be aware, the Local Government and Housing Committee is currently carrying out an inquiry into social housing supply. We were disappointed that the Development Bank of Wales (DBW) declined our invitation to provide written or oral evidence, on the basis that the Bank “currently supports small house and commercial property developers across Wales”, but is “not active in the social housing sector”.

We note, however, evidence which suggests that the DBW is active as a funder of social and affordable housing within multi-tenure residential developments. This evidence includes the DBW’s annual report for 2022-23, which states that a total of £48.3 million was invested across its residential and non-residential property funds, delivering 163 homes, 28 (17%) of which were affordable.

The Welsh Government has also signalled an intention for the DBW to play an active role in financing social housing supply. In response to a question in Plenary on 17 October 2023, the First Minister confirmed that the Welsh Government already uses the DBW to fund social housing construction, and that the then Minister had asked the DBW to “do more work in this area”.¹

In this context, we would therefore be grateful for your response to the following points:


¹ Plenary, 17 October 2023, Record of Proceedings, paragraph 71

- Could you confirm what communications have taken place between the Welsh Government and DBW about doing 'more work' to fund social housebuilding, as the then First Minister stated in plenary on 17 October 2023.
- Could you set out whether DBW seeks to influence the percentage of social and affordable housing that forms part of the developments it funds? Could more be done to increase the proportion, given that on average 17% of the homes delivered on sites funded by DBW were affordable in 2022-23?
- What potential is there for DBW to expand lending directly to housing associations and community-led housing initiatives to fund social housebuilding?

As we are nearing the end of our inquiry, we would be grateful to receive a response to these points before the end of August.

I would be happy to meet, should you wish to discuss any of the above in further detail.

Yours sincerely



John Griffiths
Chair

Croesewir gohebiaeth yn Gymraeg neu Saesneg.

We welcome correspondence in Welsh or English.

John Griffiths
Chair, Local Government and Housing Committee
Welsh Parliament,
Cardiff Bay,
Cardiff,
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27th August 2024

Dear John,

Firstly, I would like to apologise for any disappointment caused because of us not attending or providing written evidence to the Committee. The initial terms of reference we reviewed focused on the delivery of new build social housing, which we have limited involvement in. However, your subsequent questions highlighted the Committees interest in affordable housing, which we are pleased to respond to in more detail.

Before answering your specific questions, it may be worthwhile setting out DBW's involvement in the delivery of affordable housing which is directly linked to our support for SME developers who are building new housing for private sale at full market value.

Our support to SME developers is driven by the failure of private market finance support to this part of the sector, where most traditional lenders (e.g. high street banks) withdrew in the aftermath of the "credit-crunch" financial crisis of 2007–2008 and related changes to capital adequacy ratios (Basel III regulations in 2009). This created an access to funding issue that led to a significant reduction in new SME housing developments across the Welsh housing market and an over-reliance on national/plc housebuilders to meet new private sector housing needs. DBW identified this market failure and worked alongside the Welsh Government to help address this access to funding issue by creating specific funds that offer commercially priced, repayable loan funding to SME developers to support their delivery of more private market housing schemes in Wales.

Many of these private market schemes include an Affordable Housing requirement, which is set by the Local Planning Authority through a Section 106 Agreement. These Agreements are made following viability assessments and related negotiations between the housebuilder and Local Planning Authority. Where Affordable Housing requirements are agreed, these will typically result in a proportion of the houses on site being restricted to a below market sale (or rental) value – meaning those units can only be sold/rented for 80% (sometimes less) of their open market value.

A condition of DBW's funding support for housebuilders is full planning approval being in place for the scheme in question, meaning DBW currently has no influence in the planning process nor related Affordable Housing negotiations (as these take place prior to our involvement). DBW does, however,

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include support for related build costs of Affordable Housing through our loans to SME developers for their private market schemes. Indeed, we actively encourage SME developers in Wales to consider schemes with Affordable Housing requirements on the basis that we will offer the necessary loan funding support. This often requires a higher Loan to Value ratio than would have traditionally been available (e.g. >70%), which DBW's loan funding has been designed to accommodate.

Therefore, whilst DBW has no direct influence on the determination of Affordable Housing requirements agreed via the planning process, our loan support to SME developers does help support the delivery of more Affordable Homes in Wales.

Social Housing is Local Authority and/or Registered Social Landlord owned. Our understanding is the building of new Social Housing is funded through a Social Housing Grant, which is delivered directly by Welsh Government to the LAs/RSLs in Wales.

To date, DBW has not been involved in the delivery of any new build Social Housing funding in Wales and therefore has limited direct involvement in the sector.

There are two exceptions:

1. On some of the housing sites we fund, the LA/RSL will sometimes offer to purchase several units from the SME developer for use as Social Housing (despite them being intended for private sale). This may be at a discounted value or at full value – this is determined by commercial negotiations between the developer and LA/RSL (i.e. not subject to a Section 106 or other formal planning agreement). DBW is not involved in such negotiations but notes that the prevalence of such examples has increased over recent years. This may be linked to the greater emphasis on LA/RSLs to deliver more Social Housing.
2. We are aware that some RSLs have created commercial entities (e.g. sister businesses) to complement their Social Housing activity with some private market activity. Business models in this space vary but will typically see private market profits used to support increased delivery of Social Housing by the RSL. These arrangements can help the economics of Social Housing delivery as less grant funding is needed; the private housing elements can be commercially funded (e.g. by DBW) and return a profit that helps pay for the Social Housing units. DBW has some limited experience in this space but would be open to working more broadly with the Social Housing sector on similar models if this was something Welsh Government wanted us to pursue.

In response to your specific questions:

1. Could you confirm what communications have taken place between the Welsh Government and DBW about doing 'more work' to fund social housebuilding, as the then First Minister stated in plenary on 17 October 2023.

The property team in the Development Bank are in constant communication with colleagues in the Housing, Local Government and Planning department regarding existing property funds and other initiatives including schemes to improve energy efficiency in Welsh homes, the leaseholder support scheme and other proposals aimed at increasing housing supply and

affordable homes. These discussions are ongoing and have resulted recently in the launch of the Green Homes Wales scheme.

2. Could you set out whether DBW seeks to influence the percentage of social and affordable housing that forms part of the developments it funds? Could more be done to increase the proportion, given that on average 17% of the homes delivered on sites funded by DBW were affordable in 2022-23?

As set out above, whilst DBW has no direct influence on the determination of Affordable Housing requirements agreed via the planning process, our loan support to SME developers does help support the delivery of more Affordable Homes in Wales. Our residential housing funds include support for build costs of new Affordable Housing on private market sites, which offers positive influence via the SME developers we support. However, DBW is not involved in the setting of Affordable Housing requirements, which forms a key part of the upfront planning and viability process.

Given that provision of Affordable Housing is based on the viability assessment approach, it seems the only sustainable way to increase Affordable Housing delivery in the context of the private sector would be to improve the commercial viability of such schemes.

Such viability has suffered considerably in recent years, as reflected in JLL's recent reporting citing that the cost of delivering new build housing has increased by 35% over the last 5 years (compared with a 21% increase in house prices). This disparity is largely the result of macro market events that resulted in major inflation to the cost of labour and materials. The limited availability of new sites being released for development over this period has also seen significant inflation in the cost of development land. Influencing labour and material costs is difficult due to the complexity of contributing global factors. However, we identify two potential opportunities to address this viability issue:

- a) *Influence the release of more land for SME development. Publicly owned sites could be released for private market sale at a lower than market value subject to quid pro quo conditions relating to greater levels of Affordable Housing than would be set through Section 106 Agreements. This would see an increase in provision of housing on both sides of the market, but with delivery being fully funded through private/commercial funding (no grant funding required). This is something DBW would welcome involvement with.*
- b) *Offer subsidised funding (potentially via DBW) to SME developers for building sites with a greater level of Affordable Housing than would be stipulated through planning.*

In both cases, conditions could also specify the need for full integration of Affordable Housing on such schemes (i.e. so they are unidentifiable from their private market counterparts), thereby increasing both the number and quality of Affordable Housing units being delivered.

3. What potential is there for DBW to expand lending directly to housing associations and community-led housing initiatives to fund social housebuilding?

Subject to demand for finance and available funding there may be a role for the Development Bank in direct lending to support social housebuilding. We refer back to our earlier comments regarding the commercial entities RSLs have created, which could be supported by DBW.

I hope this helps the inquiry and would be very happy to arrange a meeting if there were any issues you would like to discuss further.

Yours sincerely,



Giles Thorley
Chief Executive