Housing Partnership Canada

August 3, 2016

Dear Minister Morneau,

Housing Partnership Canada ("HPC") is a pan-Canadian network of large non-profit housing organizations focused on bringing the best ideas to the operation of housing organizations and seeking new ways to meet our mandates. We are pleased to submit the following pre-budget submission for your consideration.

HPC appreciates the progress your government has made on its commitment to supporting affordable housing in the 2016 budget. We also appreciate your efforts to develop a National Housing Strategy. We are supportive of your goal to build stronger communities by ensuring that investments "help the social housing sector achieve self-reliance" and meet our shared goals of sustaining safe, healthy and affordable communities.

Our recommendations below outline ways you can support this in Budget 2017:

(1) Maintaining current investment in support of social housing:

As the social housing sector forges a path towards greater self-sufficiency, we must address the toll that years of declining investment has taken on the supply of social housing. Continued investment will preserve an increasingly scarce resource and lay the groundwork for the future. Therefore, we urge that the government commit to:

- Halt further reductions in social housing spending
- Maintain the estimated $1.5 billion currently directed at social housing
- Engage with other levels of government, and stakeholders such as HPC, to identify how best to deploy these funds to maintain the financial viability of existing social housing, and to encourage new models for the delivery of community housing.

(2) Long-term commitment to capital support for new affordable housing:

We applaud the government's commitment to the IAH program in 2016. IAH provides a capital base that leverages Provincial and Municipal funds, which is essential to making housing affordable. Low-cost, long-term financing is essential to the production of new affordable housing. We urge the government to:

- Continue this commitment through the IAH or new structures developed as part of a long-term National Housing Strategy
- Ensure access to capital is aligned with the structures developed for the delivery of loans through the proposed Infrastructure Bank so that the two elements of housing finance work in tandem and over the same time periods
- Utilize the housing sector-created Canada Housing Finance Authority (see below) to deliver and secure loan capital to the housing sector

(3) Infrastructure investment for renewal and new development of affordable housing:

HPC members welcome the inclusion of social infrastructure in the ten-year infrastructure plan and the proposed Infrastructure Bank, a key piece that supports the delivery of new infrastructure. Of equal importance will be the development of programs and structures that leverage government investments and attract new capital.

The diverse financial needs of affordable housing projects, developing new capital and risk models, and managing a varied array of projects - both in size and complexity – make access to financing a challenge for the sector. HPC has worked to examine the feasibility of creating a dedicated lending institution for affordable housing providers to finance the regeneration and development of their assets. The proposed Canada Housing Finance Authority ("CHFA") would focus on pooling capital requirements of a diverse group of affordable housing providers and provide access to capital lending markets efficiently and cost-effectively.

As the attached Feasibility Study Summary indicates, the CHFA is a viable model for achieving our shared goals. But its success requires support in several key areas. Based on our findings, we urge the government to:

- Provide credit support/guarantee of $100 million to the CHFA to set a loan target of $1 billion and achieve a desirable credit rating, thereby enabling it to take advantage of longer-term funding and provide customized terms for borrowers
- Assist with startup costs to establish the CHFA
- Establish a formal, cooperative commercial relationship with CMHC to ensure that appropriate projects are selected and financing programs effectively integrate, are non-competitive and support the self-sufficiency of the sector

The CHFA affords the government an opportunity to reach and positively impact more communities across Canada than traditional funding or subsidy programs. It also continues the affordable housing sector on the path towards greater self-sufficiency.

We welcome the opportunity to discuss the recommendations above in greater detail.

Sincerely,

Shayne Ramsay
Chair, Housing Partnership Canada
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Canada Housing Finance Authority (CHFA)

Our vision is to create a dedicated lending institution for affordable housing providers across Canada to finance the regeneration and development of their housing projects. Dedicated entirely to the housing sector, it will help providers become more financially self-sufficient, and provide the opportunity for organizations to effectively meet affordable housing demands in their communities.

Background

In 2015, Housing Partnership Canada (HPC) undertook to perform a feasibility study to assess the need, shape and scope of a dedicated lending institution for affordable housing providers across Canada. The study was conducted by Morrison Park Advisors (MPA) and funded by 17 federal, provincial, local organizations. The first phase of this study is now complete. The following provides a summary of the findings.

Addressing the Need

The need for such an institution grows out of the current state of Canada's affordable housing sector:

- **The current funding model falls short:** The sector is facing a multi-billion dollar unmet capital funding need. Government subsidies, grants and revenue tools cannot cover these capital requirements.

- **Providers must unlock and leverage equity in existing assets but lack adequate tools to do so:** Due to the fragmented nature of the sector, most housing providers lack the knowledge and scale to carry out complex financial transactions and to bear their costs.

- **Limited access to lenders:** Lenders have been challenged by the complexity of the sector – different jurisdictions, provider sizes and ownership structures – to offer a large-scale financial solution.

- **Sector Self-Sufficiency:** A dedicated lending institution will support providers in developing credit-worthy business cases that result in sustainable housing portfolios.

MPA estimated the total capital requirement for the next 10 years to be between $77 billion and $121 billion based on publicly available studies, private publications, and the CMHC housing database. This confirms that demand for capital is significant, growing, and outstrips government funding capacity (including CMHC direct lending, provincial funding, and municipal funding) by billions each year.

Proposed Structure

To address this gap, the study recommends creating a Canada Housing Finance Authority (CHFA). Under the proposed model, the CHFA will aggregate the borrowing needs of participating housing providers and fund them through the Canadian debt capital market, offering providers access to unsecured, fixed low-cost long-term financing.

To attract private investment capital, the CHFA, participating housing providers and their housing assets must be considered creditworthy by the investment community, earning an "investment grade" credit rating from a credit rating agency. The study proposes three key requirements to achieving this:

1. A large, diverse loan portfolio of high-quality assets or development projects that generate a stable, reliable cash flow stream to cover the cost of operation and debt service payments will be needed.

2. Borrowers will need to create sound business plans and demonstrate ongoing commercial discipline. The CHFA would be responsible for requiring and monitoring this discipline.

3. Government support will be required to assist the CHFA in achieving the desired credit rating.

As a sector-based financing vehicle, the CHFA would provide expertise in housing development and regeneration, finance, and underwriting required to bridge the gap between housing providers and debt investors. While there is large unmet demand from Canadian debt investors for creditworthy infrastructure investments, most do not have expertise in the needs of affordable housing providers. At the same time, most housing providers do not have the expertise to access the capital markets on their own. Beyond bridging this gap, the study speaks to the imperative for housing providers to become more financially self-sufficient as they work to address affordable housing demands in their communities. The study concludes that in order to be effective, the CHFA must also focus on:

a) Creating more user friendly (ie flexible and/or streamlined) lending products; and
b) Delivering practical management tools to make the financing process easier.

The CHFA would complement the work of CMHC in two key areas:

1. Channel federal investments more quickly and directly to qualified housing providers by helping navigate interjurisdictional and sector complexity – programs to support areas which federal policy might target – for example, improving energy efficiency, creating more mixed-income communities or seniors' housing.

2. Support the work of the CMHC Affordable Housing Centre in helping the private, public and non-profit sectors develop housing that does not require ongoing federal assistance. CHFA would enable rigorous and sector-specific due diligence on investment opportunities.

To assist in determining whether the sector has the financial viability to raise third party debt, a subset of housing providers were asked to submit high-level project data. In total, 21 municipalities or housing providers submitted development project data. Combined, the funding requirement was nearly **$1 billion** comprising **73 projects** and over **7,700 units** of both new and regenerated housing.

Proven Models

MPA focused on three market precedents for the CHFA:

- **The Housing Financing Corporation (THFC)** - a dedicated UK financial intermediary for the social housing sector that borrows from banks, the capital markets and the European Investment Bank and re-loans to UK housing associations.

- **Toronto Community Housing Corporation (TCHC) -** raised $250 million in 2007 and another $200 million in 2010 from the debt capital market. TCHC has a credit rating of AA- from S&P.

- **The First Nations Finance Authority (FNFA)** - a not-for-profit Canadian organization that provides low-cost loans, investment options, and capital planning advice to First Nation governments. FNFA has strong federal government support, including a $10 million Credit Enhancement Fund that can be used to support FNFA's financial obligations.

Based on these precedents, and assuming the combination of government support and structure of CHFA is sufficient to earn an investment grade credit rating, MPA concludes that investors in the Canadian debt capital market should be willing to deploy capital into the affordable housing sector. With the support of the federal government, the CHFA could effectively serve the unmet capital and organizational needs of housing providers and provide efficient, reliable access to low-cost capital.

Conclusions

There is a large unmet need for capital to regenerate and redevelop existing social and affordable housing and to meet significant demand for new units. The CHFA can build on existing market precedents to provide attractive long-term financing at competitive rates. The CHFA would also offer several additional benefits:

- Housing providers would be able to achieve their objectives more easily;
- Debt investors would access a new Canadian infrastructure asset class that can provide attractive financial returns and compelling social returns;
- Government would achieve meaningful results in the regeneration of existing social and affordable housing; and
- The CHFA would serve as a powerful example of harnessing private capital in order to meet a public need.

Government support will be necessary to earn an investment grade credit rating, which is required to attract debt capital market investors. The design of the CHFA should include a strong set of structural credit support mechanisms and sufficient government support to earn an investment grade credit rating. Feasibility will be further enhanced by the active involvement of CMHC.

Key Considerations

- **Federal Support to Establish the CHFA:**
    - Federal support will be necessary to earn the investment grade credit rating required to attract debt capital market investors. In particular, ***we believe that a form of first loss guarantee may be more efficient than an actual funding amount, and propose that CMHC serve as guarantor***. We would expect to work co-operatively in optimizing the form, terms and conditions of this credit support mechanism.
    - We estimate that start-up costs of up to $3 million will be incurred over a two to three year period, with the majority being required in year 1. ***We propose an initial operating grant of $1.5 million to fund half of CHFA's startup and operating costs*, *with a potential source of funding from the announced $208.3M Affordable Rental Innovation Fund.*** This would signal a meaningful federal commitment and would enable HPC to gain commitments from the national affordable housing sector to fund the remaining 50%.