PAYING FOR PUBLIC PROJECTS

FUTURE OF LONDON

ABOUT FUTURE OF LONDON

Future of London helps build better cities through knowledge, networks and leadership – across disciplines, organisations and sectors. We are the capital's independent network for regeneration, housing, infrastructure and economic development practitioners, with 4,000+ professionals using FoL as a hub for sector intelligence, connection and professional development, and a mandate to prepare the next wave of cross-sector city leaders.

PROJECT TEAM

Amanda Robinson, Nicola Mathers, Lisa Taylor, Charli Bristow

PROJECT PARTNERS

We are grateful to Montagu Evans, Poly UK, and Lewis Silkin for supporting this work.

Montagu Evans is a property consultancy run by a team of partners. A group of individuals that are outstanding together. We care about people. About legacy. About spaces to live, work, communicate and connect.

Poly Developments and Holdings Group is one of the largest Chinese company principally engaged in in the design, development, construction and sale of residential and commercial properties, as well as the provision of property management services. Poly UK focuses on London and UK markets.

Lewis Silkin's recognised experts provide legal services in all major service areas. Their clients range from small businesses to FTSE 100 companies, all who value their personal touch, their effective communication, and their individual style.

CONTENTS

INTRODUCTION

2019 was a tumultuous year for public sector finances. At the national level, a constantly shifting Brexit date, complex Brexit arrangement terms, a rotating roster of ministers, another general election, a sudden Public Works Loan Board interest rate increase, and continued tinkering with business rates created an uncertain environment for delivering public housing, regeneration, and local infrastructure projects.

Meanwhile, willingness to take action against the climate crisis and growing demand to generate greater public benefit from development – from forward-thinking public sector organisations, investors, developers, and residents – is driving changes in how public projects are financed and delivered.

To help find a way through the tumult, Future of London's Paying for Public Projects programme set out to identify trends, risks, and opportunities across financing and funding streams, based on real-world experience and expertise.

This briefing brings together desk research and insights from three cross-sector senior roundtables, held throughout autumn 2019 (see **Appendix B**). It includes:

- A snapshot of financing and funding sources for public projects (specifically housing, regeneration, public realm, and local infrastructure schemes)
- Financing/funding trends in London
- Barriers to public organisations accessing or implementing sources and possible solutions
- Possible future directions for public project finance

We are grateful to project sponsors Montagu Evans, Poly UK, and Lewis Silkin for hosting and input, as well as the roundtable participants who offered their time and expertise.

DEFINITIONS

In this briefing, **public sector** refers to local authorities, the Greater London Authority, Transport for London, and housing associations.

Financing is how organisations meet the upfront costs of building a piece of infrastructure, while **funding** is how the operation and maintenance of the infrastructure is paid for throughout its lifecycle.[1] For a list of financing and funding sources, refer to **Appendix A**.

The briefing focuses on financing and funding for public infrastructure projects such as housing, regeneration, public realm, and local infrastructure schemes, but not large-scale projects such as Crossrail or HS2.

TRENDS

Roundtable discussions and desk research revealed key trends for London's public sector financing and funding landscape.

INNER VS OUTER LONDON

In recent years, investment and development have shifted from inner toward outer London. In terms of housing, in 2015/16, inner London had roughly 12,360 housing starts; outer London had around 9,600. By 2018/19, inner London starts fell to 5,310 – a 57% drop – while outer London held steady with 9,660 starts.[2] Some outer boroughs are more prepared for and amenable to this influx than others.

A DO-IT-YOURSELF APPROACH

Asset management

Among both housing associations and local authorities, pressure has shifted from raising capital to securing revenue. Retaining and reusing underperforming assets has overtaken outright disposal/sale as the preferred option, as confirmed by roundtable participants. In many cases, this also drives a broader social and local economic agenda.

One of the most prevalent scenarios has been repurposing vacant or underused buildings as affordable workspace or for community benefit. For example, Poplar HARCA's 'Open Poplar' initiative allows local people, businesses, and social enterprises to pitch ideas for disused spaces such as garages and storage units, and receive subsidised space if their plans include activities to benefit the community. In LB Haringey, the Green Rooms Art Hotel is a council-owned building run by a workspace operator. The space provides 80 beds aimed at travellers from creative industries, open rehearsal space, and a kitchen with six-month residencies providing business support for up-and-coming restaurateurs.

Development

Among councils holding onto assets, some are also taking a lead in development, such as by commissioning developers to deliver schemes, arranging joint ventures (especially for large schemes), or, increasingly, delivering their own council homes.

One local authority participant outlined their self-financing model, wherein the council borrows via its General Fund, Housing Revenue Account, or Public Works Loan Board to finance estate regeneration. Schemes contain a mix of council homes and shared or private ownership; income from private sales and social rent is used to repay loans over 40 years and subsidise social housing.

This model gives a lot of control to the borough, but requires high land values and house prices, making it more effective in inner than outer London. However, as inner London property values stabilise, construction costs increase, and outer boroughs draw developers, this option may become less viable and top-ups from central government grant funding necessary to achieve viability.

USING GRANTS & OTHER SOURCES

Grants

Throughout the last decade of relentless government funding cuts, London has suffered the worst: in terms of absolute cuts, London has seen £3.9bn removed from services spending – accounting for 30% of all cuts in the UK.[3] Central government makes alternative capital grant funding available through departments such as the Ministry of Housing, Communities, and Local Government (MHCLG), intended to pump-prime sites for development and attract private investment. The Greater London Authority (GLA) and European Union also offer grant funding.

However, councils, housing associations, and delivery partners all occasionally decline funding due to onerous conditions, unrealistic targets, or heavy admin burdens. For example, requirements to spend funding or start/complete a project within a specific timeframe are often a major constraint to accessing such funds. One public sector body walked away from £250m of Housing Infrastructure Funding because it couldn't meet the tight conditions, and has since shifted strategy to work with central government landowners.

New uses for existing sources

In addition to redeploying land and assets, some well-known finance and funding sources are being used in new ways. For example:

- Section 106 contributions arranged as long-term, annual payments (i.e. as revenue) instead of one-offs (i.e. as capital)
- Local government pension funds investing in projects in employees' own places of work/living; for example, three local government pension bodies in London are planning to launch a new investment fund which will focus on assets in London[4]
- Central government pilot allowing local authorities to retain a higher proportion of business rates

The rates pilot could result in a sizeable income stream: London's business rates are projected to top £8bn for 2019/20.[5] However, concerns abound, including the complexity of the system being piloted;[6] costs associated with the appeals process;[7] higher rates driving away or killing businesses;[8] and boroughs outside London or with fewer businesses becoming 'have-nots' when the current redistributive system disappears.[9]

THE RISE AND FALL OF THE PUBLIC WORKS LOAN BOARD

The Public Works Loan Board offers Treasury-issued loans pegged to government bond rates. They are popular because of their low interest rates and straightforward, few-strings-attached issuance process, though they have reasonably large early repayment penalties. PWLB loans comprise some 75% of borough borrowing across the country.[10]

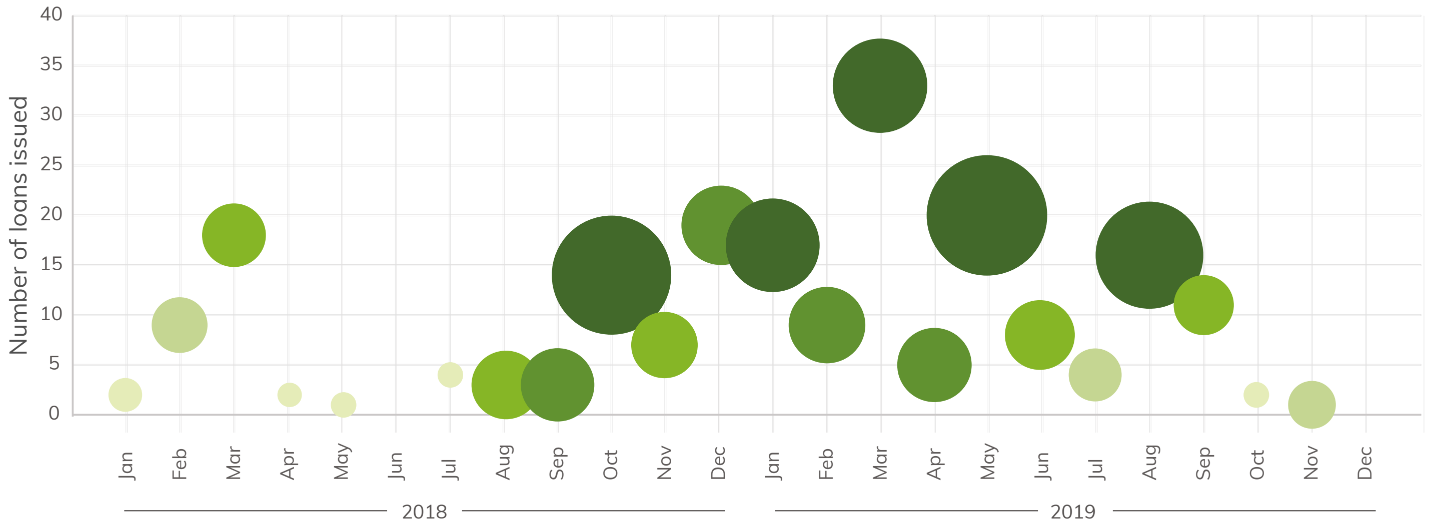
In October 2019, the Treasury raised all interest rates by one percentage point overnight. Although this only pushed rates back up to autumn 2018 levels in terms of total cost of the loan, the change took the public sector by surprise, throwing plans into disarray. It appears to have led to a drastic drop in PWLB borrowing (which could also have been affected by the general election announcement a few weeks later and ongoing Brexit uncertainty). Among London's public sector, use of the PWLB ground to a halt with the rate hike.

Local Government Association members have reported the rate increase will impact housing and regeneration schemes in particular.[11] Councils are unlikely to abandon projects, but projects on the margins of viability may no longer be viable, and councils will have to absorb the losses involved in delivering programmes set up under lower interest rates.

Ultimately, the PWLB is still among the most straightforward finance choices, though the rate increase means it may become an option of last resort.

Number and value of PWLB loans issued to London, 2018/2019[12]

n.b. includes loans to local authorities and TfL



Bubble size = combined value of loans issued

- Up to £50m
- £51m to £100m
- £101m to £150m
- £151m to £200m
- £201m+

FILLING THE PWLB VOID

The rate increase is an opportunity for local authorities to diversify their financing options, and many have started going elsewhere for money. One survey from Oct 2019 found the most popular alternative is to borrow from other local authorities (peer-to-peer lending), and that interest has grown in the UK Municipal Bonds Agency (UKMBA).[13]

Sources somewhat crowded out by the PWLB's accessibility and affordability – in particular, institutional investment for long-term borrowing, traditional banks for short-term borrowing, and municipal bonds – are keen to pick up some of the slack. A number of these sources are also attractive because they do not attract 'minimum revenue provision', an accounting measure by which public bodies must write down the principal debt over the course of the loan.

UK Municipal Bonds Agency

Established in 2015, the UKMBA intended to offer an alternative to the PWLB for local authorities, but as of publication was only just preparing to launch its first bond.

Municipal bonds tend to be high value (£250m+) and require credit ratings, but UKMBA aims to reduce barriers to entry and keep the process quick and affordable. UKMBA has its own credit rating system as well as standardised documents and processes. Organisations needing smaller sums can 'pool' with others with a good credit rating; those needing larger sums can go it alone using UKMBA's standardised process or pursue bonds through the commercial market.

Institutional investment and banks

Institutional investors – insurance companies, pension funds, asset managers, etc – are attracted to long-term projects in the public sector, especially organisations with low debt-to-operating ratios, because they offer security and fixed rates. These investors have significant sums ready to invest.

The more forward-thinking institutional investors are looking beyond financial returns to social impact and forging partnerships with boroughs to deliver regeneration at scale.

For short-term borrowing (i.e. loan terms up to five years), public organisations can approach traditional banks, who are keen to reconnect with the public sector and support infrastructure and regeneration projects.

CHANGING ECONOMY

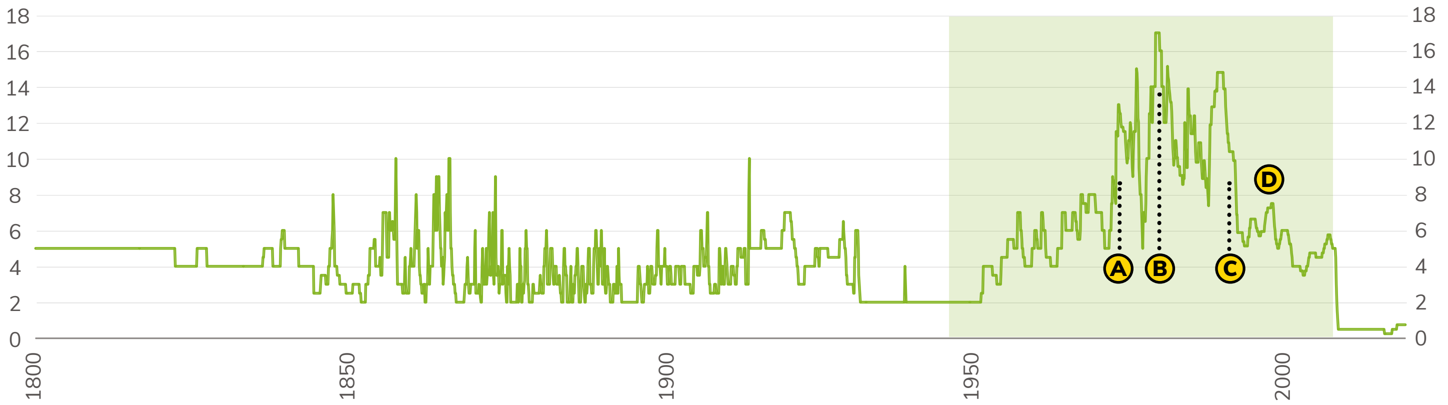
Professor Yolande Barnes, Chair at the Bartlett Real Estate Institute, suggests that the economic conditions of the late 20th century were a historical oddity and have come to an end. High inflation, high interest rates, and capital growth from high-value assets has given way to lower inflation (through rising global supply of goods), falling interest rates, and pressure on assets to 'create income streams (so institutions can pay their pensions) rather than just grow in value.'[14]

With property price increases slowing, growth will increasingly come from occupier rents rather than land value ('occupier' being someone who rents a home, or entities renting retail, commercial, industrial or other buildings). This points towards an economy where real estate acts as a 'service': responding to what occupiers want and need from a building; generating ongoing income for owners/investors; and requiring active stewardship and maintenance.

At the same time, political events throughout the last four years indicate appetite among voters across the spectrum for different approaches to governance and the economy.

Historical Bank of England interest rates[15]

n.b. rate was 5% from 1719 to 1800, and between 3% and 5% from the Bank's inception in 1694.



Post-WWII to 2008 recession

A 1973-75: recession and high inflation

B 1980-81: recession and all-time high interest rate of 17% as Thatcher govt attempts to curb inflation

C 1990-03: recession and high inflation

D May 1997: new Blair govt raises rates until Sep 1998

CHANGING CLIMATE, CHANGING ATTITUDES

The role of the financial system in the climate crisis is under increasing scrutiny. Mark Carney, Bank of England governor from 2013-2020, highlighted research showing that current pension fund investment policies will lead to a 3.8°C change scenario.[16] Given that one major insurer estimates that the world becomes uninsurable with a 4°C change,[17] this is a dangerous investment strategy.

Organisations around the world have taken note of climate impacts on markets. Investors are showing interest in 'temperature scores' to indicate how much their portfolios contribute to climate change,[18] as well as the potential for 'social bonds' issued by local authorities or housing associations.[19]

Fossil fuel divestment is also releasing enormous amounts of money that will need to be redirected. For example, Ireland's divestment was worth €68m.[20] BlackRock, which made headlines in January 2020 for committing to divest from companies generating more than 25% of revenue from coal, has $1.8tn in actively managed funds.[21]

Local authorities are also following suit, with pension fund divestment underway in Southwark and Islington. More broadly, many have also declared climate emergencies, though they are still getting to grips with how to fund and determine planning specifications for environmentally friendly development.

If public sector actors and their delivery partners can position themselves as more socially and environmentally conscious investment choices, they stand an excellent chance of attracting some of that wealth.

CHALLENGES

As seen above, public sector organisations have a variety of options for financing and funding. They also face a variety of challenges in deploying them effectively. Changing and conflicting politics at all levels can create unstable environments. Risk avoidance tends to drive the public sector towards tried-and-tested sources, leaving new and emerging sources for the bravest organisations. The scale of a project can also present challenges; projects in the £5m to £15m range in particular often fall into funding gaps, or require complex and sometimes awkward partnerships to attract grants.

Underlying all this is a lack of skills and knowledge, which came up repeatedly in roundtables. Improving public sector understanding of development finance options – and helping the private sector understand public finance, project processes and constraints – is critical to effective project delivery.

POLITICS

National level

Government

At the national level, frequent changes in political and policy direction means local authorities constantly have to pivot or lose progress.

National grants are linked to national policy objectives, which may differ from local ambitions. Grants can support a borough's vision in some ways (e.g. increasing social and affordable housing) but could dilute the vision if a borough has to shoehorn in unneeded initiatives to satisfy national policy aims. Grants also require monitoring, which takes resource.

Treasury

Dealing with the Treasury is another stumbling block. With Treasury's focus on land value uplift as the basis for awarding grants, organisations whose schemes focus on social, economic, environmental, or wellbeing outcomes find it challenging to align their project valuation to the Treasury's narrow definition of value. For one borough applying for the Housing Infrastructure Fund, the immense environmental benefits of a large-scale regeneration scheme were left out of the bid in favour of focusing on land price increases.

It remains to be seen whether the government's 'levelling up' agenda – to raise economic opportunities throughout the UK outside of London – will address the rigidity of land value uplift assessment criteria.

One participant pointed out the stifling effect the Treasury can have on London: "London's problem is that the value added of any infrastructure project we wish to undertake is going to be overwhelmingly positive, and the majority of land value added is abstracted to the Treasury." Ultimately, London and other municipalities are 'stuck with a finite pool of genuine local authority local revenue'.

> "Constant changes to [Community Infrastructure Levy] and [the National Planning Policy Framework] aren't helping because whenever boroughs take a step forward and start making progress on schemes, you get central government saying 'you need to fund education', or 'you can pool Section 106 again', and it feels like you're going back a mile. It throws all your cards up in the air."
>
> – Public sector roundtable participant

Borough level

Local authorities can also find themselves split or swapped between political parties from one election to the next. Constant change can mean incoherent policy and governance, which risks putting off potential partners.

One roundtable participant noted the legal wrangling required to extract a client from a joint venture which soured after an unexpected political change; another pointed to LB Hackney as an example of a 'stable' borough in terms of governance and politics, which have laid the groundwork for steady and coherent growth.

RISK AND REPUTATION

Risk aversion in the public sector cuts across departments, from finance to housing to regeneration and beyond. Public sector actors must choose funding sources carefully, since they can't afford for projects to go wrong: few have the reserves to experiment or reattempt failed projects, nor can they be perceived as burning through taxpayer money.

However, respondents pointed out that high risk aversion can be a risk in itself, potentially side-lining impactful projects or effective partnerships. For example, one participant noted that foreign investors can struggle to open a dialogue with UK authorities, as the source of money is closely scrutinised. Non-profit and third sector partners may also be viewed as risky.

The riskiness of sources can change over time, as illustrated by the falls from grace of private financing initiatives and 'lender option borrower option' bank loans.[22] Commentators have raised flags over 'income strips', concerned that commercial and retail market volatility and the struggle to find tenants for marginal properties could put public sector leaseholders out of pocket.[23] As with any arrangement, due diligence is key.

Even joint ventures, generally considered by public sector finance directors to be a 'safe' option because financial risk is shared among partners, have faced greater scrutiny in the wake of LB Haringey's aborted development vehicle and controversy surrounding the Earl's Court redevelopment. A roundtable participant facilitating a new joint venture explained that extensive termination provisions are being written into the partnership agreement – and questioned whether the developer would start to doubt the strength of the partnership as a result.

Partnerships, sponsorships, or naming rights agreements can bring reputational risk to all parties even if just one is embroiled in controversy or questionable activities. For example, arts and cultural institutions receiving sponsorship from BP have faced pressure from campaigners to cut ties with the oil and gas behemoth, and trustees have resigned in protest.[24]

INCOME STRIPS

Income strips are agreements wherein a private-sector freeholder/building owner provides a tenant (e.g. a local authority or housing association) with a 25- to 50-year inflation-linked lease on a building. The tenant receives ongoing income through sub-leasing. At the end of the lease, the tenant can buy the freehold/building for £1 or other peppercorn sum. The property can be new, but some cases involve organisations selling their own buildings (generating a quick payment) and leasing them back from the new owner.

Income strips have grown in popularity as a way for public sector organisations to raise capital and/or attract investment while receiving an ongoing net income from buildings without having to finance development. For example, L&G has invested £252m in 4,000 homes for housing association Places for People, which will lease the homes for 50 years, and sublease them to tenants.[25] Arrangements can operate outside an organisation's local area: LB Barking & Dagenham has taken on a 50-year lease of a hotel in Aldgate, predicted to earn £600k per year.[26]

Public trust

The impact of public sector financing and partnership choices on public attitudes should not be overlooked. Public trust in local authorities and developers is near rock-bottom, with both sectors viewed as focused on money over local needs.[27]

One local authority participant elaborated, saying residents in their outer London borough worry about where new buildings will fit and densification bringing a 'concrete jungle' – even though from the council's perspective, densification is planned for just 10% of the area, which will remain predominantly low-rise. It's challenging to work through conflicting perceptions, but the participant suggested being sensitive to the fact that 'residents are being asked to go on quite a long journey' with new development.

Another participant highlighted an example of rebuilding trust through co-producing a local commercial strategy.[28] Residents engaged quickly topics such as traffic, design and public realm, but initially struggled to engage on commercial matters. After building trust through co-producing other aspects of the strategy, project partner Montagu Evans instigated discussions about viability-related decisions, delivery structuring and finance options, helping residents become comfortable with technical issues and empowering them to make decisions on commercial matters.

Ultimately, financing isn't just about signing a deal, it's about making it work. Managing tensions and relationships – with partners and residents – over the long term will always be part of financing deals, so choosing the right partners and arrangement is paramount. It's up to public sector organisations to set out a clear, strong vision with local needs at its core and choose partners whose values and ways of working align with their own.

SCALE

Roundtable participants pointed out that medium-sized projects in particular (around £5m to £15m) can fall into a financing gap: too small for big pots of central government funding and institutional investment (which tend to operate in the £50m+ and £250m+ ranges respectively); too big for Section 106 contributions or revenue from council assets and levies.

Scaling up smaller sources to cover major schemes is a challenge, but they are useful leverage to attract additional money. For example, one respondent noted that although borough-run lotteries bring in relatively small amounts, councils have full control over it, and it can make all the difference to a project in attracting more funds. Another suggested a tourist tax to help pay for maintenance of public realm and amenities in tourist hotspots. Crowdfunding has also become widespread, specifically for grassroots organisations seeking seed funding.

Smaller, community-level projects can benefit from local authority support or funders who operate on smaller scales, but traditional banks and investors are unlikely to get involved. Big Society Capital is trying to fill the gap, investing in projects under £10m to support proof of concept and take on initial risk. Once a project is stable BSC can help bring in partners and scale up financing.

There is also the matter of spatial scale, wherein boroughs or housing associations struggle to coordinate financing when assets or projects are scattered throughout an area. Working with banks or financial advisors could help identify ways to pool mid-size financial needs and access a wider range of borrowing options.

LOCAL LOTTERY

Local lotteries operate similar to national lotteries. LB Harrow started a weekly community lottery in 2019. Of each £1 ticket, 20p goes towards prize draws, 20p to admin, and 60p to local causes. Local trusts, charities, and community groups can register as causes, and players can choose to either support a specific cause or a general fund distributed by LB Harrow.

TOURIST TAX

Tourist taxes are levies on visitors collected by a municipality through accommodation, tours, or entrance fees at tourist attractions. They are widely used in other cities or countries.

GLA research indicates tourist tax on accommodation could generate between £42m and £364m yearly depending on the tax structure.[29] Mayor Sadiq Khan, as well as 2020 mayoral candidates Sian Berry (Green) and Shaun Bailey (Conservative), have all expressed interest in a tourist tax for London.[30]

CROWDFUNDING

Crowdfunding is money raised from individuals or organisations through online platforms, sometimes matched by a public body. Within the built environment, funds support local-level schemes and social initiatives.

This is one of the most successful sources to emerge in recent years, with support from the GLA and several local authorities supplementing individuals' contributions. For example, the Peckham Coal Line is a community-led project to create a walking and cycling link in Peckham through disused railway infrastructure, shown at right. Through the Mayor's Crowdfunding Campaign, the project raised £65,000 from more than 900 local people and £10,000 each from LB Southwark the GLA to undertake a feasibility study. The Coal Line now forms part of Southwark's Local Plan.

PRECEDENT

While there are plenty of financing and funding sources available, lack of precedent for how to access and implement them slows uptake – and low uptake means a lack of expertise and best practice set precedent. This conundrum applies a learning curve to a wide range of sources.

For example, the previous section discussed bonds, institutional investment, and banks – all long-standing options, but all recently overshadowed by the Public Works Loan Board. Using these sources will require public sector organisations to arrange credit ratings and different legal agreements or covenants.

In London, only the GLA, TfL, and LB Wandsworth have obtained credit agency ratings,[31] so while it isn't unheard of, it is new territory for most public organisations. To reduce barriers to entry, the UKMBA assigns an internal credit rating to borrowers and some institutional investors are following suit.

Lack of precedent has also affected Community Infrastructure Levy (CIL) income. Over the last decade, boroughs have amassed CIL, but many lack the governance structures and knowledge to dispense it appropriately.

More knowledge- and experience-sharing could help, such as through guidance or forums. For example, Transport for London, which sets policies for and administers Mayoral CIL,[32] runs a pan-London CIL Collection Group where TfL and boroughs can share and discuss best practice on spending borough CIL and Neighbourhood CIL.

Emerging sources

If the public sector struggles to deploy well-known sources like bonds and CIL, lesser-known and emerging sources are at more of a disadvantage and risk being overlooked. For example, green bonds are gaining traction with other national governments, but the UK government has lagged behind, leaving it to city-level entities like TfL and Swindon Borough Council to test the waters (see overleaf).

EMERGING SOURCES

Green bonds

Green bonds function like regular bonds, but are used to fund sustainability projects and may be issued in lower amounts. TfL issued a £400m green bond in April 2015 to help finance low-carbon transport projects, such as low-emission buses, cycling improvements, and line upgrades. TfL's treasury team drove the process, getting buy-in from the Board, senior management, and other departments. Upon issue, the bond attracted global investors and was oversubscribed by 50%.[33]

On a more local scale, Swindon Borough Council issued a £1.8m bond in 2016 to complement £3m of borough funding to build a solar farm. Rather than target large investors, Swindon used an online peer-to-peer investment platform to allow local people to invest as little as £5 into the project for a 6% return. Of the 708 investors, around 1/3 were from the Swindon area. The solar farm can supply 1200 homes and save 2000 tonnes of CO_2 per year.[34]

Islamic finance

As investment in line with Sharia law, Islamic finance cannot charge interest. Instead, banks use arrangements such as purchasing assets and reselling or leasing back to buyers; working in partnership with clients to share risk and profit.

Islamic finance has supported major schemes like Vauxhall/Nine Elms/Battersea, the Shard, and the Olympic Athlete's Village. Islamic banks have large sums to invest, but generally lend for under five years rather than the long-term scales regeneration requires. With traditional banks, peer-to-peer lending, or the PWLB offering more familiar routes to short-term loans, there are no incentives for the public sector to approach Islamic banks; for now, Islamic finance and public infrastructure projects remain largely off one another's radar.

Municipal cryptocurrency

Municipal cryptocurrencies could step in where cuts to traditional sources threaten to squeeze services and project delivery. Many cryptocurrencies (or 'digital currencies') are based on blockchain, a decentralised database/ledger in which all transactions are recorded, accessible and uneditable – and therefore seen as transparent and secure. Berkeley, California is setting up a cryptocurrency municipal bond, in which residents can invest to help finance affordable housing, public realm, and other services.[35]

SKILLS & KNOWLEDGE

Having the right skills is critical to choosing the right financing and funding options, establishing effective partnerships, and minimising risk.

Extensively discussed at all three roundtables, the issue of skills and knowledge cuts across many of the above challenges. Although skills gaps are usually attributed to the public sector, politicians and private sector teams also have much to learn.

Public sector

> "It's not just about commercial skills when it comes to accessing funding. There's a deficit of skills in most local authorities in writing business cases. With the Future High Streets Fund there have been 100 grants for £150,000 to develop business cases for high street investment; the majority of that £15m is going to consultants. ... Even if there were just an understanding of the process and why business cases are important, I think that would lead to more intelligent commissioning and probably save money."
>
> – Private sector roundtable participant

Roundtable participants acknowledged the lack of development finance, business case preparation, and partnership management skills within local authority and housing association teams. In some organisations, lack of data about the assets they own is also a problem.

Without the right skills and knowledge, public sector teams risk missing out on funding and financing options and effective partnerships. It also means more money spent on consultants.

Getting the right skills

Pointing towards endless budget cuts, public sector representatives noted they struggle to hire staff with commercial skills in the face of higher private sector salaries. One participant suggested restructuring salary hierarchies: "Certain skills command a premium: a chief executive doesn't need to be the most highly paid person in the organisation."

Non-salary benefits like training programmes (which could be commissioned with other organisations), access to senior mentors, flexible working, and good pension schemes could also attract people; joint hires could help spread the cost of skilled staff; or career swaps could give employees experience of working in a different sector.

Using funds appropriately

The Ministry of Housing, Communities and Local Government (MHCLG) is also aware of the skills gap. MHCLG grants – which would ideally be used for pump-priming – have in some cases gone towards infrastructure that would have been better delivered by the private sector. MHCLG knows that some boroughs lack capacity to attract private money and stand their ground in partnerships, but expects some of their grants to go towards long-term upskilling within teams.

Confusingly, it's the Department of Culture, Media and Sport which has a 'social investing' team to help boroughs map capacity deficits and understand what's needed for effective partnerships and to successfully attract funding.

Understanding procurement

Finally, many roundtable participants felt uncertain about how to navigate procurement and unclear on when a project needs a full tender process. Some felt that current requirements make it difficult to have pre-procurement conversations with potential partners, noting that procurement teams can put the brakes on a project just as much as financial teams.

Elected members

Getting councillors on board is necessary to push through schemes, but they also need upskilling to be able to ask the right questions – of developers and planners; about development finance and partnership options; and on behalf of residents – such as through neutral or independently developed induction courses. Particularly if councils start issuing bonds, elected members need to understand disclosure obligations and timelines for issuing, which may require a faster pace than other council operations.

Private sector

The skills gap cuts both ways. Private sector partners often don't understand public sector accounting; one public sector roundtable participant explained that financial modelling has been brought in-house because consultants didn't understand local authority legislation and processes.

Rekindling relationships between banks and public sector organisation needs attention. Banks see the public sector as a safe option for low-risk, short-term lending, but need greater understanding of how public organisations operate – along with recognition that reserves, stability, and ambition differ from one to the next.

To facilitate better understanding, the public sector needs to offer a strong vision and business case for a project; allow time for financial, regeneration, and housing directors to develop face-to-face relationships with lenders or private sector partners; and keep them informed of changes. The process isn't as quick as borrowing from the PWLB, but it builds connections and trust.

WHERE NEXT?

It's clear that London's finance landscape is evolving, but predicting the forms it will take is no easy task. However, major changes and trends – namely, a new majority Conservative government and an increased willingness among many organisations to act on climate change – offer clues for key areas to watch.

NEW GOVERNMENT, NEW DIRECTIONS?

Although murmurs from the Conservative party during the December 2019 general election hinted at the end of the austerity spending policies of its predecessors,[36] recent instructions for ministers to cut budgets have muddled the party's messaging.[37] In terms of other policies and the 'levelling up' agenda, it's still too early to say at the outset of 2020 what form they will take and whether they will have any meaningful impact on public funding and financing.

One area to watch is devolution. During his time as Mayor of London, Boris Johnson supported greater devolution to London and other cities and city-regions. As Prime Minister with a majority government, he can now make it happen.

Further devolution, especially fiscal devolution with attendant powers, will benefit London[38] – but the public sector needs staff skills and time to make the most of it.

CLIMATE-CONSCIOUS INVESTMENT

Given growing action towards the climate crisis, divestment and responsible investment will gain pace. Public sector organisations play a key role in driving change. They can:

- Take advantage of investor appetite for secure, long-term, sustainable income by positioning themselves as investment options that align with positive environmental and social outcomes
- Divest employee pensions from funds with fossil fuels in favour of sustainable funds and local development
- Use their purchasing power to be ruthless about choosing partners and investors with demonstrated strategies for achieving net zero

CLIMATE-CONSCIOUS DEVELOPMENT

> "How long is [growth] going to go on for? Growth is great in the medium term, and it's necessary to replenish the workforce, but in the long term – looking towards 2050, 2070, and the end of the century – we have to think about whether it's a sustainable model. ... These questions about how big London really gets will start to emerge in the next five to ten years."
>
> - Public sector roundtable participant

Squaring the climate crisis and urban development is a critical issue.

Growth can generate additional investment and tax revenue. However, accommodating the additional people, buildings, and infrastructure necessary to support growth puts pressure on London's built and natural environments – and developing these buildings and infrastructure is currently a hugely carbon-intensive process.

It's imperative that future public projects are delivered with climate change in mind, from selecting financing streams to construction to lifetime operations. The public sector has a major role to play, reducing emissions through internal working practices, procuring the right partners, and selecting responsible financing options – and the private sector must prepare to follow suit.


CORAL
Londis
CORAL
Santander
20808
Santander

APPENDIX A: SOURCES

Public bodies use a multitude of sources on any given project. The list below captures many recurring sources as well as lesser-used sources with potential for wider uptake.

Scale of sources (n.b. most on a per transaction/project basis; * indicates per year basis):

£ = up to £10m
££ = more than £10m, but less than £250m
£££ = £250m or more

Source	Scale	Information
Central government programmes		
Public Works Loan Board (p. 3, 4)	££–£££	Treasury-allocated loans for local authorities, popular for financing housing and regeneration schemes as well as helping boroughs buy commercial or other property as investments
Housing Infrastructure Fund (HIF) (p. 6)	£–££	Grants for housing projects and associated infrastructure necessary to support housing (e.g. utilities, flood defences), with grants allocated based on proving land value uplift to the Treasury
High Streets Fund/Towns Fund	£–££	Grants to regenerate high streets; its cousin, the Towns Fund, operates similarly but on a town-wide scale
Local growth funding	£	Grants for local economic partnerships to deliver employment opportunities
Shared Prosperity Fund	£££	Ministry of Housing, Communities, and Local Government (MHCLG) initiative intended to replace EU funding at the end of 2020
Business rates retention pilot (p. 3)	££–£££	Initiative allowing some local authorities to retain 100% or 75% of their business rates
Greater London Authority programmes and options		
Affordable Housing Programme	£–££	For registered providers to build more affordable tenure homes
Council Homes for Londoners	£–££	For councils to build their own housing for social rent
Strategic Investment Fund	££	GLA initiative to use its share of London business rates (via the business rates retention pilot) to create a £112m fund for key projects
Local levy	££–£££*	Special short-term levies added to council tax to raise funds for projects, e.g. Olympic Games levy
Borough options		
Council tax	£££*	Property taxes on homes which goes into the General Fund
Business rates (p. 3)	£££*	Property taxes on businesses, which were traditionally fed to central government for redistribution, but are now being retooled and devolved to allow boroughs to retain 75% to 100% of income
Section 106 (p. 3)	£–££	Cash contributions paid by developers to local planning authorities, intended to be spent on local infrastructure and initiatives. While contributions are usually one-off, some boroughs have arranged long-term, annual contributions.
Community Infrastructure Levy (CIL) (p. 6, 9)	£–££	Introduced by central government in 2010 to allow local authorities to collect money from development to fund new infrastructure
Housing revenue account	££*	Income from rents and services associated with local authority-owned housing, which is ring-fenced for building and maintaining housing. Councils can borrow against their HRA.
Other rental income	££*	Income from other borough-owned assets (e.g. shops, garages)
Asset sale (p. 2)	£–££*	Income from selling land/assets and right to buy

Source	Scale	Information
Parking fees	£–££*	Income from controlled parking zones, workplace parking levies, car parks, and parking fines; much goes towards road safety programmes, road maintenance, and concessionary fares
Self-financing (p. 2)	£–££	Local authorities borrowing from themselves (e.g. through Housing Revenue Account, General Fund) to finance regeneration/housing schemes, and paying back the loan through sale of private and shared ownership housing
Peer-to-peer lending	£–££	Boroughs lending to one another, often to fill short-term cash flow gaps
Land value capture (p. 6)	££	Borrowing against projected future land values (and property sale prices) to finance a project
Tax increment financing	££	Borrowing against projected future business rates income to finance a project
Bonds (p. 4, 9, 10)	£–£££	Issued by cities to raise money for projects; bond holders (investors) lend money to the city and receive repayments with interest over time. 'Green bonds' function the same but raise money for green infrastructure and may seek lower amounts of money than traditional bonds.
Private institutions		
Institutional investors (p. 4, 5, 7)	£££	Investment from insurance funds, pension funds, asset managers, etc, usually for long-term projects, especially housing projects
Banks (p. 4)	£–££	Lending from traditional banks, usually for periods up to five years
Sponsorship/naming rights (p. 7)	£*	Funding for ongoing operation in exchange for branding e.g. TfL Cycle Hire (Santander), Emirates Air Line
Islamic banks (p. 10)	£££	As investment in line with Sharia law, Islamic finance cannot charge interest. Instead, banks use arrangements such as purchasing assets and reselling or leasing back to buyers; working in partnership with clients to share risk and profit. Used in a small number of regeneration schemes in London.
Private individuals		
Philanthropy	£	Donations from high net worth individuals
Crowdfunding (p. 8)	£	Money raised from individuals or organisations through online platforms, sometimes matched by a public body. Within the built environment, funds support local-level schemes and social initiatives.
Lotteries (p. 8)	£	Money raised from public lotteries (e.g. Heritage Lottery Fund) and distributed to local projects
Other		
European Union	££–£££	Grants for projects across member states, which will be replaced by MHCLG's 'Shared Prosperity Fund'
Joint ventures (p. 7)	££–£££	Partnerships between public and private organisations (usually developers or investors); public organisations provide land while private partners bring capital, commercial skills, and development expertise - and development risk is shared across partners
Foundations & trusts	£–££	Grants from charitable organisations e.g. family trusts, livery companies, private trusts, corporate foundations
Income strips/lease wrappers (p. 7)	££–£££	Agreement wherein a private-sector freeholder/building owner provides a tenant (e.g. a local authority or housing association) with a 25 to 50 year, inflation-linked lease on a building. At the end of the lease, the tenant can buy the freehold/building for £1 or a similar peppercorn amount.
Tourist tax (p. 8, 9)	£-££*	Levy on visitors collected by a municipality through accommodation, tours, entrance fees etc, which is spent on public realm maintenance or other initiatives

APPENDIX B: EVENTS

In addition to desk research, this project consisted of three senior roundtables, held throughout October and November 2019. Participants representing a range of organisations were invited to discuss the following topics and questions.

Roundtable 1
Public sources

Online summary: bit.ly/32mZ4eL

Q1 What public sources of funding/financing are you using or have you encountered? What are the benefits?

Roundtable 2
Private sources

Online summary: bit.ly/2uuF7q6

Q1 What private sources of funding/financing are you using or have you encountered? What are the benefits?

Roundtable 3
Emerging sources

Online summary: bit.ly/37XJ6ZM

Q1 What emerging/alternative sources of funding/financing are you using or have you encountered? What are the benefits?

Questions at all roundtables:

Q2 What are the political and financial risks of these sources? How can they be de-risked, at least partially?

Q3 What skills and expertise are needed for more effective funding/financing efforts and project delivery?

Q4 How has use of these sources evolved, and how might it change in the short term (1 to 2 years) and mid term (3 to 5 years)? What factors have driven/are driving this change? What other public sources are on the horizon?

ENDNOTES

1 For more information, see Institute for Government bit.ly/2SVf9nO and bit.ly/2V6zj0N

2 MHCLG Table 253: permanent dwellings started and completed, by tenure and district. Inner/outer London definitions follow those used in the London Plan. Some figures imputed by MHCLG in the data table. bit.ly/32d7gyj

3 Centre for Cities, Cities Outlook 2019, 29 Jan 2019. bit.ly/2wpO6JB

4 Colin Marrs, Room 151. "Pension bodies team up to create London housing and infrastructure investment super-fund," 20 Jan 2020. bit.ly/37PeaLu

5 UK Government, 2020. National non-domestic rates collected by councils in England: forecast for 2019 to 2020. Accessed Jan 2020. bit.ly/2PaSra4

6 Colin Marrs, Room 151. "MPs: Government must consider alternative to 'risky' business rates retention," 21 Aug 2019. bit.ly/2uRU71x

7 Dominic Brady, Public Finance. "Concern over business rate retention proposals," 22 Feb 2019. bit.ly/3bXfpeS

8 Stephen King, London Councils. "Business rates," 2 May 2019. bit.ly/2wyXieT

9 Hugo Bessis, Centre for Cities. "London shouldn't be allowed to keep all its business rates – yet," 26 Oct 2017. bit.ly/2SMH3nj / Neil Amin Smith, David Phillips and Polly Simpson; Institute for Fiscal Studies. "100% business rates retention may lead to divergences in English councils' funding without promoting growth," 1 Mar 2018. bit.ly/38LqKMO

10 Naomi Clayton, Simon Jeffrey, Anthony Breach; Centre for Cities. "Funding and financing inclusive growth in cities," 13 Dec 2017. bit.ly/2SInhce

11 As reported by Sarah Pickup, Deputy Chief Executive, LGA at EY's Local Authority Funding Forum, Jan 2020. See 'Setting the Scene' video at bit.ly/2V9Hb1p

12 Debt Management Office, Public Works Loan Board historical data. Accessed Jan 2020. bit.ly/2V6uNiX

13 Colin Marrs, Room 151. "Councils to seek PWLB alternatives to maintain capital programmes," 24 Oct 2019. bit.ly/37OHrG9

14 Yolande Barnes, UCL Bartlett Real Estate Institute. "A view from the Chair: Green infrastructure means business," 11 Apr 2019. bit.ly/2HGdZat / Josephine Smit, Housing Today. "Interview: Yolande Barnes, Bartlett Real Estate Institute," 8 Apr 2019. bit.ly/2ViLCYb

15 Rates from 1694 to 2013 from The Guardian Datablog, "Interest rates in the UK since 1964," 10 Jan 2013. Rates from 2013 onwards from Bank of England database, "Official bank rate history," bit.ly/2uTz5j4.

16 Roger Harrabin, BBC News. "Bank of England chief Mark Carney issues climate change warning," 20 Dec 2019. bbc.in/2T4PwRo

17 Michael Holder, GreenBiz. "AXA: 4C warming makes the world uninsurable," 18 Dec 2017. bit.ly/2SIDZs3

18 Simon Jessop, Matthew Green; Reuters. "Climate change pushes investors to take their temperature," 20 Jan 2010. reut.rs/2V9PFFU

19 Sarah Williams, Social Housing. "Prepare for 'massive swing of capital' seeking impact, sector told," 6 Dec 2019. bit.ly/2PaccyO (paywall)

20 Charlie Taylor, Irish Times. "Republic withdraws public money from fossil fuel investments," 4 Jan 2019. bit.ly/2PbXMy5

21 Tim Buckley, Tom Sanzillo and Melissa Brown; Energy Post EU. "$7tn investor BlackRock announces Coal divestment, but not across all funds," 20 Jan 2020 bit.ly/2V91En6

22 Long-term bank loans, usually around 50 years, wherein lenders can impose higher fixed rates at certain dates and borrowers must either accept the new rate or repay the loan. Local authorities haven't pursued LOBOs since 2012. For more information, see on.ft.com/2HGfaXr

23 Judith Evans, Financial Times. "The local government gamble on commercial property," 23 Nov 2018. on.ft.com/2V4mfJn / Colin Marrs, Room 151. "Councils warned over 'son of LOBOs' income strip deals," 4 Apr 2019. bit.ly/39TtiZF

24 BBC News. "British Museum trustee resigns over BP sponsorship and repatriation," 16 Jul 2019. bbc.in/2SJRFmQ / BBC News. "Mark Rylance resigns from RSC over BP sponsorship," 21 Jun 2019. bbc.in/37HYglX

25 For more information see Luke Cross, Social Housing. "Analysis: what does the future hold for the leaseback?" 1 May 2014. bit.ly/38MTYLw (paywall) / Josh Rose-Nokes et al, Savills. "Spotlight: Private Money and Affordable Housing," 4 Dec 2019. bit.ly/3bXjRKC

26 Colin Marrs, Room 151. "Council enters hotel business in investor-backed income strip deal," 20 Mar 2019. bit.ly/2V6wOvn

27 A Grosvenor survey from summer 2019 found only 2% of the public trust developers to act in an honest way and 7% trust local authorities to make decisions in the best interest of an area. See Rebuilding Trust, bit.ly/2T0ilP1

28 "'Co-production' refers to a way of working whereby citizens and decision makers … work together to create a decision or service which works for them all. The approach is value driven and built on the principle that those who use a service are best placed to help design it." Skills for Health Toolkit, bit.ly/2T355cf

29 Matthew Daley, Greater London Authority. Options for a tourism levy for London: A publication for the London Finance Commission, Jan 2017. bit.ly/32g7bdk (PDF)

30 London Green Party, Mayor & Assembly Manifesto 2016. bit.ly/32a76HO / Cathy Adams, The Independent. "London mayoral candidate pledges to introduce tourist tax in capital," 10 May 2019. bit.ly/2vLsqY9

31 Mark Sandford, House of Commons. Local government in England: capital finance; briefing paper number 05797, Oct 2019. bit.ly/2HLRrFb (PDF)

32 Like borough CIL, Mayoral CIL is calculated and collected by local authorities. Since April 2019, Mayoral CIL has been used to fund Crossrail 1 and 2. For more information, see the GLA's website bit.ly/32aSJDe

33 Climate Bonds Initiative, "Case study: TfL Green Bond," date unknown. bit.ly/2HJRXU8 (PDF)

34 Abundance Investment, "Swindon Common Farm Solar CIC" bit.ly/37LEiqg / Michael Benke, Swindon Advertiser. "Clock is ticking on solar investment scheme," 17 May 2016. bit.ly/2V3eyTM / Lee Boyce, This is Money. "Would you invest in a council-backed solar farm for a 6% return?" 23 Feb 2016 bit.ly/1oAxkxY

35 Sarah Holder and Linda Poon, Citylab. "Why Do Cities Want Their Own Cryptocurrencies?" 20 June 2018. bit.ly/2V3NOm9

36 Dearbail Jordan, BBC News. "Chancellor Sajid Javid declares end of austerity," 4 Sep 2019. bbc.in/2T4B384

37 George Parker and Chris Giles, Financial Times. "Johnson and Javid order budget cuts of at least 5%," 29 Jan 2020. on.ft.com/2wzTdan

38 For more information about fiscal devolution for London, see the London Finance Commission paper Devolution: a capital idea, Jan 2017. bit.ly/37JQ2Tf (PDF)

ACKNOWLEDGEMENTS

Paul Augarde, Coherent Cities; **Ken Baikie,** Notting Hill Genesis; **Karen Barke,** LB Lewisham; **Yolande Barnes,** Bartlett Real Estate Institute; **Gemma Bourne,** Big Society Capital; **Charles Butters,** Poly UK; **Sarah Cary,** LB Enfield; **Hayley Collen,** Epiphron Limited; **Graeme Craig,** TfL Commercial; **Lorena Farias,** TrustBlock; **Rick Gibbs,** Burnden Capital; **Neill Gibson,** Trowers & Hamlins; **Pete Gladwell,** L&G; **Matt Hemsley,** MHCLG; **Jimmy Huang,** Poly UK; **Owain Jones,** LB Lambeth; **Jonathan Martin,** LB Waltham Forest; **Oliver Maury,** Montagu Evans; **Catherine Max,** Catherine Max Consulting; **Paul Munday,** Funding Affordable Homes Housing Association; **Chris Paddock,** PRD; **Naisha Polaine,** Department of International Trade; **Clare Reddy,** Lewis Silkin; **Jenny Rydon,** Montagu Evans; **Andrew Sivess,** Greater London Authority; **Jeremy Skinner,** Greater London Authority; **Javin Solanki,** Poplar HARCA; **Adam Swersky,** LB Harrow & Social Finance; **Simon Theobald,** LB Hackney; **Chris Twigg,** Inner Circle Consulting; **Anthony van Hoffen,** Lewis Silkin; **Alex Valenzuela,** South Bank Employers Group and South Bank BID; **Josephine Vos,** Transport for London; **Michelle Warbis,** MHCLG; **Luke Webster,** Greater London Authority; **Kevin White,** Montagu Evans; **Sarah Wilks,** Transport for London; **Justin Zhang,** Poly UK

Future of London helps build better cities through knowledge, networks and leadership – across disciplines, organisations and sectors. We are the capital's independent network for regeneration, housing, infrastructure and economic development practitioners, with 4,000+ professionals using FoL as a hub for sector intelligence, connection and professional development, and a mandate to prepare the next wave of cross-sector city leaders.

Future of London
70 Cowcross Street
London EC1M 6EJ

futureoflondon.org.uk
@futureofldn
Future of London