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Leveraging assets to reduce borrowing costs - experience from the Co-operative Housing Finance Society in the UK

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CHFS was set-up in 1997 to do 3 things:

- to make it easier for new housing co-operatives to raise mortgage finance for new developments
- to reduce the margin on mortgage loans to new housing co-operatives
- to reduce the costs associated with setting-up mortgage loans for housing co-operatives



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It does this by doing 3 things:

- by enhancing the credit rating of loans to housing co-operatives by providing lenders with a twelve month mortgage interest guarantee;
- by standardising loan documentation and procedures to reduce the cost of raising mortgage finance, and
- by offering improved risk management through quarterly performance monitoring of CHFS guaranteed co-ops.



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It achieves this by **leveraging** primary housing co-op assets in the following way:

- loans are secured on the **Open Market Vacant Possession** value of the co-operative's housing assets
- this enables **capital housing subsidy** to the co-operative to be used as security for the interest guarantee.



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Why?



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Because commercial mortgage lenders:

- do not like “non-recourse loans”
- do not like lending to new organisations without a business and management track record
- do not want the task of monitoring a portfolio of relatively small commercial loans
- do not want the job of sorting out the risk of default should a breach of loan covenants occur



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How?



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Worked example: (Minster Housing Co-operative, Kent)

Development costs:	£2,316,012
Capital subsidy:	£1,047,292
Net cost (mortgage):	£1,268,720
Open Market Value (OMV):	£2,272,000
Written-down OMV (72.5%):	£1,647,200
Residual equity (OMV- mortgage):	£ 378,480
12 months interest (7.123% 1999):	£ 82,678
Ratio – 12 months interest to residual equity =	4.58:1



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The costs:

- 0.5% of mortgage principal charged and paid into CHFS guarantee fund
- 0.25% annual guarantee fee
- 0.5% of annual 12 month interest payable as annual fee to Co-operative Bank plc
- 0.25% payable to the bank as commitment (not utilisation) fee
- small risk monitoring fee payable to CHFS





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The benefits:

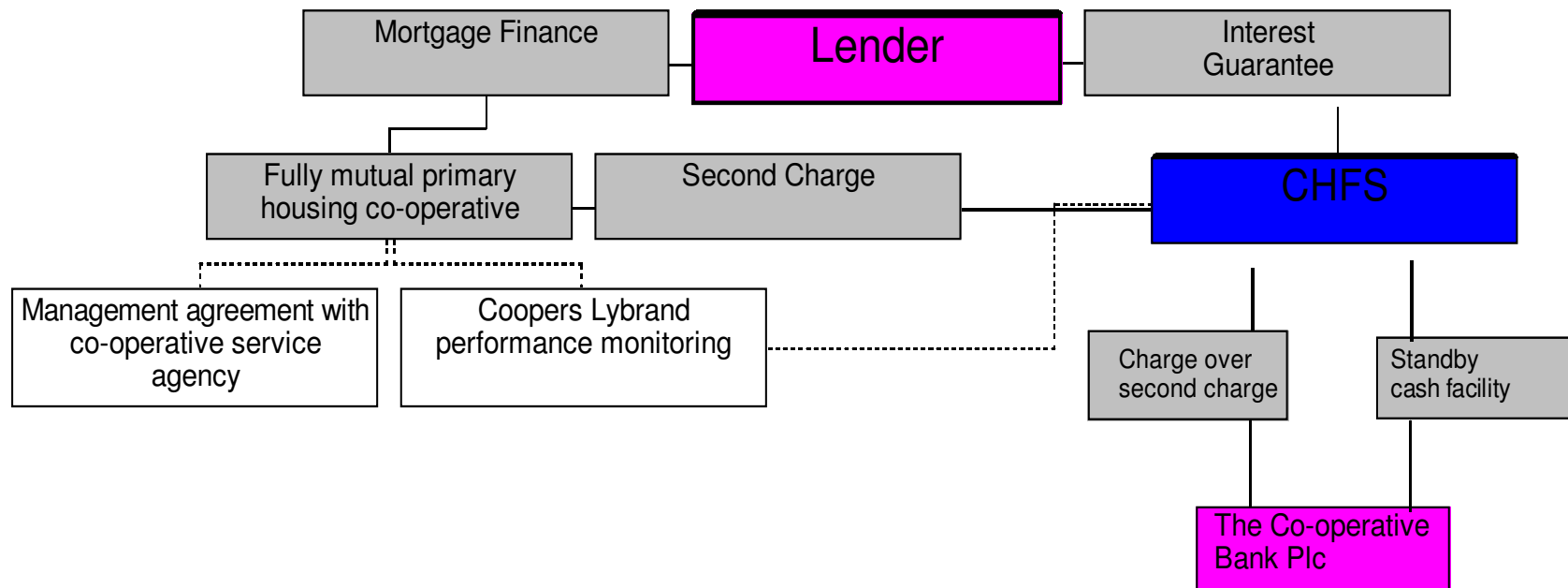
- interest rate margins are lower – typically 0.85% over base rather than 1.5%
- set-up costs are lower
- loan documentation is standardised
- burden of annual monitoring of risk and administration of the loan is easier
- **net savings for Minster of approx £5,500 per annum (£3 per household per week)**





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The legal structure:





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Where did the idea come from:

CHF Canada! Mortgage Guarantee Fund





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The lessons:

- leverage your assets to arrange finance and reduce borrowing costs
- look to examples in other countries and adapt to meet your housing finance needs
- work to overcome concerns of commercial lenders and make lending for co-op housing an attractive commercial proposition



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Where next?

- CHFS to accept investments and become a prime lender in its own right
- source ethical investments for new co-operative housing projects
- lending to mutual home ownership projects
- possibly using innovative mortgage financing such as the Canadian capital index linked loan

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Micro-finance: Solutions for Housing



International Co-operative
Alliance Housing Committee



Co-operative Housing Federation
of Canada