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CROWDFUNDING FOR KINGSWINFORD HEALTH HUB

"It's getting the first couple off the ground. Once you get something physical and you can say '... in Barnsley it delivered one of these', or with our project in Dudley, when you've got an image of a new health campus. Then I think you will very rapidly get that buy-in. I think it's going to be quite hard work to get the first couple of projects done. But I do believe that they will be market-making and, once the general public can see that, and you can then present something in a different area and say '… here's an image of what you will end up with. This will be a local health facility and you'll also be investing in your local health facility'. So, I think it's about giving some tangible examples."

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CONTEXT

A4.01 NHS Dudley Clinical Commissioning Group (CCG) have developed a Health Infrastructure Strategy plan that calls for the development of health hubs with primary care, operating at scale, co-located with other community and out-patient services, and replacing the current model of dispersed primary care and centralised acute care.

A4.02 One such area identified for a hub scheme is Kingswinford in order to improve the delivery of services throughout the region. The primary care infrastructure across Kingswinford faces challenges as some of the buildings need significant investment to address current standards and to meet future need.

A4.03 At present, they do not support multi-disciplinary team working and negatively contribute to a poor patient experience. The NHS England Five Year Forward View calls for larger facilities that bring together multiple services to work together to deliver better health outcomes[132].

A4.04 The Kingswinford scheme delivers the following benefits:

- Future service viability to meet increased population levels during the life of the facility;
- The facility will provide high quality services making the most efficient use of existing resources to reduce inequalities in health;
- The Hub will provide a collaborative approach to the delivery of services, across many organisations, to improve health outcomes;
- The Hub will result in services being delivered in a safe and sustainable manner; and
- The Hub will deliver services closer to the community and support the delivery of services within a patient's home.

A4.05 The scheme includes a Health Hub, Extra-Care Housing and Supported Living, Affordable Housing and Leisure Facilities.

A4.06 The healthcare elements of this development are planned to be delivered through the NHS Local Improvement Finance Trust (LIFT) vehicle that exists in Dudley, namely Dudley Infracare LIFT Ltd (LIFTCo). The funding and capital structure will require debt and equity with equity contributions from the LIFTCo including both public sector and private sector shareholders.

AIMS AND OBJECTIVES

A4.07 The aim of the project was to explore what and where the Kingswinford project, including its financial model, needed to change or to adapt in order to accommodate investment by local residents and the general public.

A4.08 Our research study with the University of Leeds forms part of a series of studies that aim to explore the potential for adopting democratic finance (crowdfunding) for the funding and delivery of social infrastructure projects. Our work with the University of Leeds focuses on a community project in Dudley in the West Midlands, which is planned to be developed through the NHS LIFT Programme.

[132] https://www.england.nhs.uk/publication/next-steps-on-the-nhs-five-year-forward-view/

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"I think the view is that if it is presented well then actually it's a very positive message [...] aligning a financial return with a health return, i.e. by funding health infrastructure through the community we've got access to that which can in turn help to improve and maintain health status. So, it's not just a pure monetary gain. It's ensuring the sustainability and security of local services and the facilities."

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A4.09 The proposition is that the debt requirement could be organised to be wholly or partly structured through a crowdfunded instrument and that this in turn will help to engender significant local support and allow the asset to deliver a health, social and financial return to the community served.

A4.10 It is also considered that this model could be scaled across the NHS LIFT programme, with 49 LIFTCos currently operating and covering 60% of the population of England. This could therefore be a significant outlet for crowdfunding of social infrastructure and in turn help to modernise the NHS Estate.

PERCEPTIONS AND PRACTICALITIES OF CROWDFUNDING

"I think the point about it is a lack of knowledge. So that, with our projects, we come to the stage where it needs some form of approval because the end results will be a facility where an NHS organization or primary care organization is going to take a lease. They need approval to take that lease. If the view is that this is not conventional in the way it's being funded, those that just aren't used to it and see it as unconventional may create a negative view on the approval process because they only like to approve things that they are familiar with. There is an education process for us internally to our organization."

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A4.11 It is considered that the key difference between bank debt and crowdfunding relates to who takes the risk and how.

A4.12 With bank debt there is an accessible pot of money provided on an on-going basis by shareholders. The bank assesses the investment merits of a project before lending an amount on what they regard as appropriate terms with the main risk management tool being the debt/equity ratio.

A4.13 Whilst (bank) shareholders are interested in the overall portfolio of projects, they are mostly unaware of the detailed terms of individual projects. The cost of capital is determined by the market for bank shares and the additional cost burden for bank customers is determined by the resource costs (mostly people costs) of running a bank, including project finance teams, etc.

A4.14 As examined in our research with Leeds, crowdfunding is project specific and facilitates individuals building a (wide) portfolio of projects. The managers of a crowdfunding business provide a high-tech software platform that can bring together lenders and borrowers, as well as assessing and categorising risks and securities.

A4.15 The observation is that crowdfunders are content with a risked return lower than a bank's fully built up return requirement so, in principle, there should be scope to utilise crowdfunding at scale because of the potentially lower total cost base.

A4.16 This needs to be tested further with crowdfunders, but the prima facie evidence from the research suggests that there is indeed a place for the crowdfunding of health and social infrastructure projects at scale.

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A4.17 As stated above there may well be a place for bank debt as the market matures and the investment sums required increase (e.g. NHS LIFT has so far delivered £2bn of infrastructure investment). This would present an opportunity for crowdfunding to be deployed as a ‘mezzanine’ layer of debt finance in the capital structure[133].

BARRIERS AND CHALLENGES

A4.18 If it is to be pursued through NHS LIFT, the Kingswinford Health Hub project will require a combination of equity and debt funding. The equity will be provided by the LIFTCo shareholders in the role of the LIFTCo as the developer. The senior debt for LIFT projects nationally has been provided through bank debt from institutions that are familiar with project finance.

A4.19 Given the focus of LIFT on improving both services and infrastructure for given geographies, however, the potential of crowdfunding to link local investment with local return on that investment is considered compelling.

A4.20 The issue to be addressed, and that has been the main focus of our work with the research team, is whether a capital structure that includes crowdfunding can provide a funding solution that is of a similar cost of capital to traditional bank finance.

A4.21 It is recognised that the affordability will need to be established across the full capital structure and so the equity returns have been modelled at a level that supports a part crowdfunded financing solution.

A4.22 The financial model built for the Kingswinford project has followed the structure of a project finance model widely adopted in the LIFT market and the wider project finance industry.

A4.23 The model has been constructed to show cash-flows over a 25 year term. The costs within the model include:

- Build costs;
- Equipment costs (Group 1 equipment or fixtures and fittings supplied and fixed by the contractor);
- Fees;
- Land costs;
- Lifecycle costs (to include replacement of systems and services over the life of the building, e.g. lifts, heating systems etc.);
- Facilities management costs (to include maintenance of the fabric of the building over its life).

“What target returns do we need to achieve from crowdfunding, in order for it to be attractive? We think at the moment we can get it to a level where the crowdfunding element is not that much different than the blended cost of equity and debt. We haven’t completed that yet, but we know how we’re going to go about it. We’ve got the numbers in, but we’re still going to finish that off. But we feel pretty positive where we are now that the crowdfunding option will compare well with a normal funding structure.”

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A4.24 The model went through a number of iterations during the research, with the final version developed in conjunction with the research team and led by Abundance Investment. This model is currently being reviewed internally.

A4.25 The key driver for the development of this model was the required cost of debt which would be appropriate for funding through Abundance Investment as the sponsoring platform.

[133] Mezzanine debt is the middle layer of capital that falls between secured senior debt and equity. This type of capital is usually not secured by assets, and is lent strictly based on a company’s ability to repay the debt from free cash flow. It is a form of debt often used in complex private financing models.

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A4.26 The result of adopting the target return of 4.5% for a crowdfunded product via Abundance Investment produced an initial equity return of also approximately 4.5%, if the target rent of £180 per m^2 was adopted. This was not considered acceptable to equity and so a re-calculation of the rent was undertaken based on achieving the minimum acceptable level of equity returns.

A4.27 Through discussion with equity it was determined that a minimum target return of 8% could be established. This had the impact of driving up the rent to approximately £220 per m^2.

A4.28 On review of current rents being paid for primary care premises, the £220 per m^2 was not considered an outlier and has been adopted in the model in order to deliver the target returns for the debt based Abundance Investment instrument and the returns for the equity sponsors of the project.

A4.29 These returns and inputs are now being used to produce and to circulate a project financial model for review by all relevant parties.

MAIN FINDINGS

A4.30 This study has demonstrated that democratic finance solutions (i.e. crowdfunding) are a viable method of financing projects delivered through the NHS LIFT Programme.

A4.31 It has also confirmed that crowdfunding is likely to have a higher cost of capital than traditional bank debt. The bank debt funding of projects in LIFT is a mature market and this helps with both cost of capital and approvals processes from credit committees in the institutions that have historically provided debt.

A4.32 Given bank debt will have a lower cost of capital, equity will need to take a view on returns in order to make projects funded through crowdfunded instruments attractive to the end-user and occupier. This is a trade-off for equity between return and scalability if crowdfunding was adopted as a positive method of delivering a social return.

"The benefits to the local population in having that combination of private care and extra care delivers an asset that actually improves primary care services locally, and so improve health status and access to health services for a population which has high health needs. Secondly, it addresses a demographic in the elders in terms of access to affordable housing. There are plenty of high-end retirement villages, but them being affordable is a difficult space. We've been able to show you can deliver that in an effective way so there is a new asset, and avoids people going into nursing homes, and avoids people going through the revolving door of health care. So that's a big tick. Third is that, because it needs primary care, then we have employment. So, there are three aspects to it."

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A4.33 Given this analysis, one route that should be considered is for crowdfunding to be included in the capital structure as a "mezzanine" level of finance. This would allow lower cost of capital bank debt also to be provided and to enable equity returns to be aligned with the development risk (planning, design and construction) being taken by LIFTCo as the developer.

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A4.34 It is considered that this route of a mezzanine layer for democratic capital should be pursued in further research for the sector.

LOOKING AHEAD AND NEXT STEPS

A4.35 The results of the model developed through the research with Leeds were presented at a meeting that had representatives from Community Health Partnerships, Dudley CCG, Abundance Investment and Dudley Infracare LIFTCo. The key assumptions and implications for each party were presented, including the impact on the overall affordability of the project.

A4.36 It was agreed that the next step would be to take the outputs from this study and incorporate into the required NHS Investment Appraisal structure and to support the production of an outline business case.

A4.37 Separate to this process, Dudley CCG are undertaking an internal exercise to determine the proposed Procurement Route for the Kingswinford Project and to confirm if NHS LIFT is to be the route chosen.

A4.38 The outputs from our research with the Leeds team are being used for this exercise and have been considered helpful in illustrating that LIFT, through adopting a crowdfunding solution, is a viable delivery and funding structure to bring the project to fruition.

A4.39 The planned timescales for this work are to confirm a procurement route by the end of December 2018 and to complete an outline business case by the end of March 2019.

CONCLUSIONS

"Yeah, I think they will [invest], because everybody loves their local hospital whether in a village community or up in Leeds, where everyone loves Jimmy's and the LGI. I think it's localism, and I think the NHS brand helps with the national element of this, which is why it aligns so well because it's unusual in having both a local and a national appeal. And people are proud of it, people believe it's theirs and I think allowing crowdfunding to increase that sense of ownership is a real positive. The other thing to say is the fact that pre-1948 there's certainly a large number of hospitals that were funded in this way. They were funded through public subscription."

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A4.40 This project with the University of Leeds team has sought to inform the debate on whether crowdfunding could be an appropriate source of debt and funding for health care projects at scale.

A4.41 In particular, the research has tested the suitability of a crowdfunded instrument for a healthcare project procured and developed through NHS LIFT. The analysis has focused on a LIFT project as this would enable similar crowdfunded instruments to be applied at scale in the market.

A4.42 LIFT is a mature procurement route with informed sources of capital available to it to fund projects. Given this position, crowdfunded instruments are being compared in terms of competitiveness with traditional bank funding.

A4.43 The Leeds research has therefore given rise to a direct comparison of the costs, benefits, and risks of crowdfunding with bank debt that, in our assessment, is both novel and likely to be market-making.