Industry Super Australia

Fixing Affordable Housing in NSW and Beyond

Prepared for NSW Community Housing Industry Council

11 August 2020

Authorship

This paper was prepared for the New South Wales Community Housing Industry Council (CHIC). However, the views expressed in this paper are those of the authors listed below and do not necessarily reflect those of the CHIC, CHIC members, the NSW Government nor Industry Super Australia, its funds or its investment committees.

The authors benefited from discussions with experts in the field of housing and homelessness policy, housing finance and urban planning, many of whom remain anonymous. Thanks so much to Dr Ian Winter - Chair of the CHIC, Wendy Hayhurst from the Community Housing Industry Association, Hal Pawson from City Futures Research Centre – University of New South Wales, Carrie Hamilton from Housing Action Network, and Michael Howell from CrossBorder Capital, John Longo from Industry Super Property Trust and Gary Weaven former Chair of IFM Investors. Special thanks to Jo McNaughton, Jackie Kimpton and Debi Bruce for their assistance with the final draft. All mistakes are our own.

Please direct questions and comments to:

Stephen Anthony
Chief Economist
P: 03 9657 4354
E: santhony@industrysuper.com

Gary Lu
Financial Analyst
E: glu@industrysuper.com

About Industry Super Australia

Industry Super Australia (ISA) is a research and advocacy body for Industry SuperFunds. ISA manages collective projects on behalf of a number of industry super funds with the objective of maximising the retirement savings of over five million industry super members.

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Stable and affordable housing is an important instrument in the fight against poverty but there are problems of shortages in Australia. This paper considers the extent of these and proposes policy options to effectively bridge that gap. The focus of this paper is New South Wales (NSW), but reference is made to Commonwealth – State funding arrangements and some alternative policy approaches which are relevant across regions.

The importance of government support for social and affordable housing cannot be overstated. It forms a critical safety net for vulnerable families and individuals and helps reduce the risk of recurrent poverty. Housing distress is detrimental to people's ability to earn, learn and contribute positively within their families and local communities and beyond.

Shortages of social and affordable housing continue to widen. The social and affordable rental housing gap in NSW in 2019 is estimated to be about **216,500 units**, and it is projected to rise by another 100,200 units by 2036.[1]

Against the measured shortages of social and affordable housing you would think that Australian governments must not be spending enough on assistance. This impression is false.

Commonwealth and state governments already spend at least **$7 billion** annually on housing in NSW. The problem is that most dollars are targeted at mum and dad investors rather than the disadvantaged.[2] The remaining dollars are spent on a 'mishmash' of disparate programs spread across layers of governments with no overarching coordination. There has been no overarching planning process for settlement in Australia since the 1990s.

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[1] Troy, L., van den Nouwelant, R. & Randolph, B. 2019. 'Estimating need and costs of a social and affordable housing delivery', City Futures Research Centre, UNSW Built Environment, UNSW Sydney.

The research has also shown that the total social and affordable housing gap nationally (for current and projected unmet need) is estimated to be 1.02 million units by 2036.

[2] ISA estimate based on total funding for NSW Department of Communities and Justice (DCJ), total Commonwealth Rent Assist (CRA) spending in NSW and the state's approximate share of negative gearing and capital gains discount that is proportional to its population. Here we are adding direct expenditures and tax expenditures by the federal, NSW and local governments where we have data. This does not include outlays on land tax exemptions for residential housing, pension asset test exemptions, any rent concessions and stamp duty concessions etc. If we included all these the final subsidy figure must be some multiple of $7 billion.

Figure 1 – Shared policy failure widening the housing gap

The key failure of existing approaches to housing subsidies is that they contribute to the widening of the housing gap.

- Federal tax incentives fuel investor demand for existing property (see Figure 1). One could be forgiven for thinking the goal of Australian government housing subsidies (negative gearing and capital gains discount) is to give high wealth, mum-and-dad investors the ability to buy multiple existing properties using debt via a do-it-yourself super fund.
- Monetary and prudential policy has also fuelled a debt-driven growth model for three decades. Easy money and prudential policies have driven a housing-finance feedback cycle that is economically inefficient, incentivising investment in unproductive activity, but strongly self-perpetuating in terms of its dynamics.[3]

How many dollars would it take to fix the affordable housing issues in NSW and beyond? It is estimated that the cost of building enough social and affordable housing in NSW to meet the shortfall (316,700 units by 2036) would be about **$3.5 billion** annually (Troy *et al.* 2019) which is only around half of the current outlays on housing.[4]

So, the key to addressing the social and affordable housing shortfall is to achieve a more appropriate re-prioritisation of the existing spending envelope. Subsidies must be better targeted

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[3] Ryan-Collins, J., 2019, 'Breaking the housing-finance cycle: Macroeconomic policy reforms for more affordable homes', EPA: Economy and Space, SAGE Publication, p.19.

Monetary policies as practiced by major central banks including the Reserve Bank of Australia (RBA) have increasingly impacted asset prices from the mid-1990s onwards as we entered the era of ultra-low interest rates. This has disincentivised business lending relative to residential property.

From the mid-1980s, successive governments, the Reserve Bank, financial regulators and major institutions themselves forgot the overriding purpose of macro prudential management. Banks do not exist to facilitate investors' speculation via the use of tax-subsidised debt. Rather, banks have a broader social licence, the flip side of their regulated "public utility" sinecure and too-big-to-fail status, requiring them and their executives to always act in the national interest.

Banks from the early 1990s were rejecting any social licence/public utility obligation to prioritise Australian settlement, family formation and business. Banks were rejecting their traditional role as 'pillars' of local communities, and active participants in social and economic participation.

Banks became by the 2000s, a conduit for wealth creation vehicle for funding mum and dad residential property investors via big leverage. At about the same time they forgot how to lend to Small and Medium Sized Enterprises (SME), stifling the most productive businesses in the Australian economy.

[4] The $3.5 billion figure is the annual funding needed in the form of government subsidies to enable the operation of new social and affordable housing in NSW.

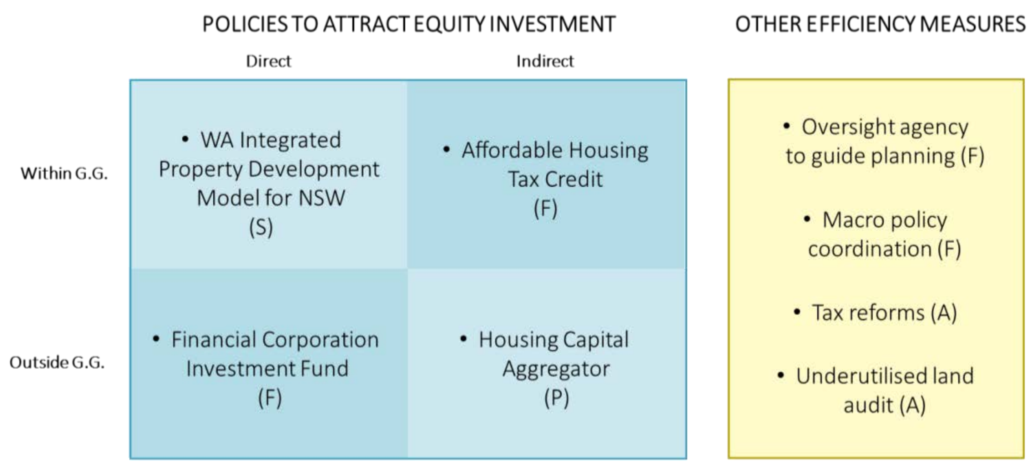
towards greenfield developments undertaken mainly by large scale not-for-profit entities such as some Community Housing Providers (CHPs). The idea is to attract enough equity investment into the sector in scale so that CHPs can leverage their balance sheets to solve the problem for Australian governments.

Attracting new equity capital into the affordable housing sector is no easy task. In this paper we explore policies and budget capacities in ways that incentivise new investment. We consider funding models with direct and indirect government involvement, with either ‘on’ or ‘off’ budget options. We also suggest structural reforms to existing policy measures to improve efficiency in property markets. These collective measures are intended to yield a stable, sustainable stream of equity funding to support project development and the ongoing operation of social and affordable housing assets.

Despite the challenges ahead, there are workable solutions to close the housing gap. We examine four proposals, at least two of which are highly promising:

1. The Affordable Housing Tax Credit – an offshoot of the cash flow tax proposed by Garnaut *et al.* (2018) that allows institutional investors to purchase tradeable tax credits in exchange for equity funding directed to regulated CHPs. This embeds affordable housing tax credit into the tax code (just like negative gearing); and
2. The Financial Corporation Investment Fund (FCIF) – an independent entity that could be established by the Commonwealth (or by state or local governments) existing outside of the general government that could invest in affordable housing developments guided by a concrete rate-of-return benchmark.

Figure 2 – Policies to attract equity investment and help to normalise property prices



Source: ISA Analysis

Note: S – state level. F – federal level. A – all levels of government. P – private sector. Horizontal categories - direct and indirect refers to the level of government sector involvement. Vertical categories - within and outside general government (G.G.) P/L or balance sheet.

We also suggest certain foundational ‘structural’ reforms to macro and microeconomic policy which might help to improve market efficiency in Australian real estate and especially in unimproved land values. These collective measures are intended to support the generation of new affordable housing projects and the ongoing smooth operation of social and affordable housing assets achieved via the normalisation of unimproved property prices across the nation over time, but especially in Eastern Australia. These policies include:

- an oversight agency to identify shortages to guide better local planning;
- coordination of macro policy supporting the goal of normalising unimproved land values over time;
- tax reforms including replacing stamp duties with and a broad land tax; and
- a full audit of underutilised land sites across Australian governments.

While the challenges are significant, the capacity for governments to deliver necessary reforms is considerable. Therefore, the reason more progress doesn't occur may be due to confusion over what the appropriate target of our existing policy should be.

In the face of the Covid-19 pandemic, it is even more essential to fix affordable housing. In 2020, Australia is experiencing the biggest peacetime health and economic shock in the global economy since the 1930s depression. In these tough times housing adequacy is no longer just about providing the most vulnerable in our society with shelter, but it has become an essential lockdown measure to keep people at home and contain the spread of the virus. People who are homeless and those living in overcrowded accommodation are among the most at-risk groups in the community, thus highlighting the need to address the matter with greater urgency.

The Covid-19 pandemic provides the urgent justification to address the 30-year decline in affordable housing as part of an effective and targeted fiscal stimulus package. But it still seems that governments are more inclined to help those who can afford to buy or renovate.

Failing to address current affordable housing supply shortfall will have disastrous intergenerational consequences. It will certainly take even more public resources to remediate these consequences. Whereas, better housing outcomes now brings with it both social and economic benefits to our local communities, improving family wellbeing, access to employment and public amenities and higher workforce productivity.

1. Introduction

Stable and secure housing provides an important mechanism for reducing some of the risks and uncertainty that contribute to the persistence of poverty. It provides a stop loss mechanism to act as a barrier against a continuing downward slide in life chances. Among the ways in which it does this is by providing the foundation for individuals to build lifelong relationships, through family and community, enabling them to achieve goals in education, employment and participate positively in local communities and broader society.

When housing access becomes uncertain and unaffordable, other misfortunes are compounded. Family relations are strained, mental and physical health is compromised, and productivity is lost. School dropout rates rise, domestic violence increases along with welfare dependency. All these misfortunes reinforce a drift into more extreme poverty which is likely to be passed through generations.

In this paper we are mainly concerned with the supply-side of housing markets, although this cannot be separated from a discussion of the causes of poverty and the role of housing to alleviate this. We leave an analysis of some of the systemic causes of poverty to a subsequent report (Coram and Anthony, forthcoming).

Unfortunately, the likelihood of housing stress is increasing in NSW because of a significant shortfall in the supply of social and affordable housing. The state's housing affordability problem has never been more acute as those in need of housing and homelessness services continue to rise. With 92 per cent of low-income private renters in Sydney now occupying unaffordable homes, and with the continued increase in the absolute shortage of tenancies within reach of this cohort[5], the situation is becoming critical. Price pressures are forcing families and the most vulnerable in our community outwards into the suburban fringe, adding disproportionate commute times to employment and social services, and increasing the frequency of relocations for those without the financial means to afford long-term accommodation. The rising tide of housing distress has causal effects on homelessness and welfare dependency.[6] Without effective intervention, these negative outcomes would be perpetuated through intergenerational poverty.[7] The supply of social and affordable housing is not keeping up with the needy, and the issue must be addressed before the problem manifests itself into a social crisis.

In order to devise better solutions to the problem, we firstly need to examine the current status of social and affordable housing funding and supply shortfalls in NSW. This paper aims to summarise evidence on the volume of current social and affordable housing stock and to identify funding and supply gaps, while also examining the current suite of funding and policy measures. Through these analyses, we hope to bring forward consideration of better public and private funding models.

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[5] Hulse, K., Reynolds, M., Parkinson, S., Nygaard, A. and Yates, J. 2019, 'The supply of affordable private rental housing in Australian cities: short- and longer-term changes', Final Report no. 323, Melbourne: AHURI.

[6] Nygaard, C. 2019, 'Social and Affordable Housing as Social Infrastructure – A literature review for the Community Housing Industry Association', Centre for Urban Transitions, Swinburne University of Technology, 7 November 2019, Website accessed 3/1/2020: https://www.communityhousing.com.au/wp-content/uploads/2019/11/Social-and-affordable-housing-as-social-infrastructure-FINAL.pdf?x33467.

[7] See Attachment C for study on potential long-term savings of adopting affordable housing as social infrastructure.

The housing supply gap

As of June 2019, the total number of social rental dwellings in NSW was 151,814, consisting of 66 per cent public housing, 31 per cent community housing, and the remainder are State Owned and Managed Indigenous Housing (SOMIH) and Indigenous Community Housing (ICH).[8]

The estimate of the social and affordable housing shortfall varies by different institutions and methodologies. According to the City Futures Research Centre, in 2019 the social and affordable housing shortfall in NSW was estimated to be 137,100 and 79,400 units respectively. The research also projected an additional 76,100 social housing and 24,100 affordable housing units will be needed by 2036, bringing the combined housing shortfall in NSW to 316,700.[9] The same research estimated that the national social and affordable housing shortfall is over 1 million units, of which NSW and Victoria make up approximately 53 per cent. As more people move into the major capital cities, the pressure on existing housing and infrastructure will get worse.

The estimated funding gap is dependent on the financial model and geographic location used in such analysis. According to research funded by the Australian Housing and Urban Research Institute (AHURI), the average funding gap for each social housing unit is estimated to be $13,000 per dwelling per year nationwide and is highly dependent on geographic location.[10] The same report estimated the supply gap for social housing in NSW by 2036 to be 212,700 dwellings, taking into account the projected increase in the homeless population and projected additional recipients outside current targeted groups.

Existing funding and policy measures

Currently, there are Federal and state level schemes running in conjunction to support the provision of social and affordable housing. Federal level programs include: the National Housing and Homelessness Agreement (NHHA); the National Housing Infrastructure Facility (NHIF); the Affordable Housing Bond Aggregator (AHBA); the Commonwealth Rent Assistance (CRA); and the National Rental Affordability Scheme (NRAS).[11] State level programs include: the Social and Affordable Housing Fund (SAHF); and the Communities Plus program overseen by the NSW Department of Communities and Justice (DCJ). Additionally, there are also policy and regulatory measures relating to planning and zoning arrangements that can be applied to add to the affordable housing stock and/or improve housing affordability, or add to the stock of affordable rental housing (at no direct cost to government) via inclusionary zoning[12].

In NSW, the funding, commissioning and management of social, affordable and homelessness housing programs has been led by the DCJ in conjunction with the Aboriginal Housing Office (AHO) and Land and Housing Corporation (LAHC). For the budget year 2019-20, contributions towards the DCJ for housing and homelessness programs consist of $485 million by the Commonwealth under the NHHA, $382 million by the state of NSW and $740 million in rental

[8] NSW DCJ 2019, *NSW Social Housing Residential Dwellings Dashboard*, Department of Communities and Justice. Website accessed 21/02/20: https://public.tableau.com/profile/facs.statistics#!/vizhome/Social_Housing_Residential_Dwellings/Dashboard.

[9] Troy, L., van den Nouwelant, R. & Randolph, B. 2019. 'Estimating need and costs of a social and affordable housing delivery', City Futures Research Centre, UNSW Built Environment, UNSW Sydney.

[10] Lawson, J., Pawson, H., Troy, L., van den Nouwelant, R. and Hamilton, C. 2018. 'Social housing as infrastructure: an investment pathway', AHURI Final Report No. 306, Australian Housing and Urban Research Institute Limited, Melbourne.

[11] The remaining incentives are being provided but the NRAS is now discontinued.

[12] Phibbs, P. and King L.A. (2018) Potential affordable dwelling yields from a NSW Inclusionary Zoning Scheme, Report prepared for Shelter NSW, University of Sydney, Sydney

revenues from the LAHC.[13] The total funding for the three state level agencies is budgeted to be around $1.8 billion.[14] Nevertheless, a measure of the scale of the funding gap for NSW public housing is the official estimate that, in 2015-16, 'the additional explicit subsidy required to fund the current difference between tenant rent contributions (including government subsidies) and market rent was $950 million per annum'.[15] [16]

Are existing policy measures adequate?

Despite the funding measures outlined above, the level of the existing supply gap and waiting lists indicates that the housing needs of many vulnerable and disadvantaged people aren't being effectively met. Allocation of resources to new public rental housing in NSW has flatlined for almost 10-years.[17] The NSW government currently expects to fund the construction of under 10,000 additional social and affordable rental homes over the ten years to 2026. But, to keep pace with growing need based on expected rates of population growth, 21,000 additional social and affordable rental homes would be needed over this period.[18]

The lack of significant net growth in social and affordable dwellings accompanied by a growing homelessness rate means currently only a portion of the accommodation needs of the homeless population are being met. Also, since the available dwellings are allocated to 'greatest needs' (or homeless) applicants, some families in less severe circumstances are being forced to wait for periods of up to 10 years to access public housing.[19] Current policies may also be (directly and indirectly) hindering the supply and demand of affordable housing. Federal Government tax policies such as negative gearing and capital gains tax discount, fuel investor demand for established properties, put upward pressure on prices and drive down rental yields.[20]

Meanwhile since the mid-1990s, monetary and prudential policy as practiced by major central banks (whilst always well intentioned), has seemingly fuelled global asset price growth and disincentivising business lending relative to residential property lending. Even though the main justification for financial deregulation in Australia was premised on expanding business lending,

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[13] Rental revenues from the LAHC includes rents received from tenants of properties managed by LAHC, but excludes rents received by not-for-profit and other providers in the system.

[14] In addition to the rental income from properties under the management of AHO and LAHC, the two agencies are also partially funded by the DCJ (through the NHHA). However cross-agency funding is excluded in the total budget of $1,797 million to avoid double counting.

[15] Independent Pricing and Regulatory Tribunal – IPART, 2017, *Review of rent models for social and affordable housing*, Draft report, Sydney, IPART.

[16] This was subsequently revised to $945 million after allowing for additional rent collection recommended by IPART - Independent Pricing and Regulatory Tribunal – IPART, 2017b, *Review of rent models for social and affordable housing*, Final report, Sydney: IPART.

[17] Presently, there's no forward commitments in new capital spending in government budgets. This is occurring while incentives such as NRAS is winding down (incentives likely to be extinguished by 2026).

[18] Pawson, H. 2018, 'Does NSW really need to double its social housing output?', UNSW City Blog, 23 June, Website accessed 7/02/2020: https://blogs.unsw.edu.au/cityfutures/blog/2018/06/does-nsw-really-need-to-double-its-social-housing-output/.

[19] Australian Institute of Health and Welfare 2018, *Housing assistance in Australia 2018*, Website accessed 26/11/2019: https://www.aihw.gov.au/reports/housing-assistance/housing-assistance-in-australia-2018/contents/priority-groups-and-wait-lists.

[20] Phillips, J., Yates, J., Krever, R., Gruen, N. & Smith J. 2015, 'Fuel on the fire: negative gearing, capital gains tax & housing affordability', Australian Council of Social Service, Website accessed 19/02/2020: https://www.acoss.org.au/images/uploads/Fuel_on_the_fire.pdf

this loan category has consistently fallen since the early 1990s as a share of total credit provision.[21]

Has the linkage between finance, communities and productivity been severed?

Historically, the business model of Australian banks was very different. It was to prioritise the efficient intermediation of capital to businesses, prioritise first-home ownership and support macroeconomic stabilisation goals. This old-fashioned view of banking – as a provider of basic services – shares many of the characteristics as a public utility (energy, water, sewerage, etc) that all households and businesses require, where quality is hard to observe, and some sort of 'state' oversight via regulatory control is often needed to prevent the abuse of power.

The banking system that arose in Australia from Federation was framed by the tragedy of the 1890s property bust and was forged under fire during the Great Depression of the 1930s, eventually informed by the 1936 Banking Royal Commission. The Australian financial system eventually emerged as a highly regulated mix of state-owned banks, some private trading banks, building societies and mutual institutions, all charged with broader development goals.

By the late 1940s, the emerging arrangements supported financial system stability by eschewing the boom-bust property credit cycle that had dominated previous credit lending - business cycles. Stability was to be brokered along Keynesian macro policy lines.

Into the post WWII world, with a baby boom underway and given a nation in urgent need of refurbishment, the local bank manager was the most important and trusted person in each town and community. Bank executives in the big cities were highly regarded by the community. But many saw this system as unnecessarily bureaucratic, old-hat and certainly not moving with financial innovations that were making the system increasingly unwieldy.

When financial deregulation finally came in late 1983, no one was particularly sad to see the old regime fall. The economy was stuck in a low productivity slump, hiding behind high and variable tariff walls. Certainly, some form of more effective economic regulation of the financial system was an essential priority. But the full-blown deregulation that occurred abandoned the development goals and hard lessons of previous generations.

So, the banking industry was handed over to the 'money changers'. Each financial institution's housing-loan book became their main game. It provided the means to cross-sell ancillary services to naive customers. Vertical integration became a deliberate corporate strategy – as monetary and regulatory policy setters conveniently accepted the security associated with industry consolidation, eventually settling on the Four Pillars policy.

The big banks moved towards oligopolistic competition in loans, up and down the household value stream – that is:

- into the payments system (credit cards), risk (life insurance and consumer credit insurance) and funds management (superannuation and trading); and
- where supply networks are captured (mortgage brokers, branch networks, financial advice).

A legacy of household indebtedness and unaffordable housing

Into the deregulated environment, the local bank branch became a shopfront with anonymous staff. Big city bank executives became very highly paid celebrities with share options. These executives apparently revelled in raising short-term shareholder value while maximising their

[21] See *Final Report of the Committee of Inquiry* - the Campbell Inquiry (1979-1981).

own compensation. They seem to have been oblivious to any notion of stewardship to their frontline employees, much less the needs of local communities.

Not too many Australians were complaining either. Bank shareholders had a very good run over the past three decades leading up to 2020. However, they may still live to regret the lack of oversight of current and past management.[22] Also, many middle-aged and older Australians have been enriched by the property cycle and this was mainly facilitated by Australian banks.

Banking funding models are changing. They had abandoned (or could no longer rely on) captive deposits anymore and so required more wholesale funding. As the community-based branch banking model disappeared, they become 'global' lenders/borrowers and dependent on collateral rather than trust, local relationships, knowledge and analysis. Collateral attracted them into the private housing market. But collateral is a procyclical factor that exaggerates liquidity cycles, making the housing market prone to more boom and bust. The result is that a long boom encouraged the public sector to withdraw from affordable housing provision. For example, in the Covid-19 downturn, they have less capacity to restart public provision of affordable housing.

The new 'incentives' driven mentality, which sprang up around major financial institutions, reawakened the old boom-bust property cycle of the pre-1940s, along with fostering an addiction to household debt that brought with it significant vulnerabilities in terms of macroeconomic management. Household debt-to-income ratios rose from 40 per cent in the early 1980s to 164 per cent before the Global Financial Crisis (GFC). Since that crisis, Australia's household debt-to-income ratio has reached a record 188 per cent – much higher than the United States' before the subprime crisis.[23]

Macro policy driving inefficient & unproductive housing investment

Monetary and prudential policy (along with fiscal policy via key tax concessions) was in the process of fuelling a debt-driven growth model which would last for three decades. Easy money and prudential policies drove the housing-finance feedback cycle that was economically inefficient, incentivising investment in unproductive activity, but strongly self-perpetuating in terms of its dynamics.[24]

National policy had effectively promoted (residential) property ownership over home ownership as the top policy priority. Financial deregulation had inadvertently prioritised mum and dad property investors relative to the goal of stable family formation and economic participation in vibrant communities. At the same time Australia's largest banks forgot how to lend to SME businesses – the engine room of productivity and future prosperity.

Having handed the RBA independence and an explicit inflation target by the mid-1990s, it is not surprising that the institution focused single-mindedly on achieving that target. So expansionary monetary policy settings (implemented mainly through cash rates or through other prudential means) intended to close output gaps and stabilise consumer prices, were spilling over to asset prices (especially in real estate). This is because housing credit was driven more by what banks

[22] The major banks' diverse nature throws up internal efficiency issues. From an external perspective, they appear to be bureaucratic and lacking an innovation culture, and this has been demonstrated by recent problems with technology, which stemmed from antiquated platforms and information systems. For example, difficulties with setting limits on cash deposits on smart ATM machines leading to lax anti-money-laundering control framework.

[23] Debt-to-disposable-income ratio sourced from DataStream/RBA.

[24] For a broader cross-country discussion see Ryan-Collins 2019.

could lever based on raising collateral and offshore borrowing, than the now antiquated notion that they would lend against their deposit base.

Policy authorities remained ultimately non-committal about the distributional merits of macroeconomic and budget policies on asset prices. Meanwhile, the young were largely locked out of the housing market, while the gains were being monopolised by existing owner occupiers and landlords, particularly in Sydney and Melbourne. Indeed, the housing-finance feedback cycle and its inequities were on the radar of then deputy Governor of the RBA, Phillip Lowe when he stated:

"Instead, what is perhaps more remarkable is the extra resources that Australian households have used to purchase, from one another, the land on which these bigger and better dwellings sit. Indeed, most of the extra money that has gone into residential property has not gone into the physical stock of housing, but rather into land. So, our fascination with housing is really, mostly, a fascination with land."[25]

Enter the Global Financial Crisis

Then from the GFC onwards, the global advent of ultra-low policy interest rates and unorthodox monetary policy and rounds of international prudential reforms has further stymied credit allocation and intermediation biased towards the most preferred collateral (real estate) and against those who are neediest (those with few assets) and/or perhaps most deserving (innovative SMEs).

- Policies like quantitative easing offshore have artificially lowered term premia on long-term borrowing, further boosting asset prices including residential property in international cities like Sydney and Melbourne.
- Policies like the Basel III and IV prudential reforms (imposing a global, voluntary regulatory framework on bank capital adequacy, stress testing, and market liquidity risk) prefer home lending over all other categories of loans.[26] This has further helped to fuel the long property boom in eastern Australia, whilst restricting business borrowing.

Central banks since the GFC have continued to remain confident in their ability to return economies to a 'steady-state' or normality.

- Meanwhile, they have been failing to achieve their inflation targets.
- They have contributed to asset price imbalances and so impacted the disadvantaged.
- Their theoretical models which rely on their ability to impact credit flows to businesses (via concepts such as the 'natural' rate of interest and money multiplier) seem now to be antiquated.
  - It seems that Fisher Black was right – money is endogenous in macroeconomic models.[27]

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[25] Lowe, P. 2015, 'National Wealth, Land Values and Monetary Policy', speech, Address to the 54th Shann Memorial Lecture, Perth, 12 August 2015. Website accessed: 27/07/2020, URL: https://www.rba.gov.au/speeches/2015/sp-dg-2015-08-12.html

[26] Warsh, K. 2014 "Rethinking Macro: Reassessing Micro-foundations," Book Chapters in Neil, M. & Taylor, J. (editor), 'Across the Great Divide: New Perspectives on the Financial Crisis', Chapter 4, Hoover Institution Press, Stanford University.

[27] Black, F. 1987, 'Business Cycles and Equilibrium', Blackwell Publishers, 1st Edition.

Summing up the role of banking in Australia

From the mid-1990s, eastern Australia experienced one long uninterrupted property boom, exacerbating affordability issues, whilst further restricting business borrowing.

Consider the loan book of major deposit-taking institutions circa March 2020:

- About 66 per cent of new lending is for housing.
- About 72 per cent of housing loans are to buy existing property.
- About 60 per cent of new loans are to investors for negatively geared investments.
- About 17 per cent of housing loans are interest only.

Direct Concerns of Community Housing Providers

Regulation and compliance duplication are noted as key concerns amongst Community Housing Providers (CHPs), while complexities in planning, construction and tenancy management adds further risk for investors of affordable housing projects.

Additionally, it is important to be aware of the impact that short-term letting (STL) platforms like Airbnb is having on the private rental market. Inner city areas are most affected as long-term rental properties are taken out of the market. These STL platforms increase the fluidity of the housing market and they also likely reduce the market's ability to provide a steady and sufficient supply of affordable housing.[28]

Exploring existing and new funding models and supportive macro / micro reforms

Having examined the current policy suite in addressing the supply gap of social and affordable housing in NSW, we present alternative funding and development models for consideration. These include the Affordable Housing Tax Credit, the Financial Corporation Fund, the Western Australian (WA) Integrated Property Development model and the Capital Aggregator model. These approaches vary according to the level of direct government involvement, they all require public subsidy to deliver the necessary outcomes.[29]

We also suggest certain foundational 'structural' reforms to macro and microeconomic policy which might help to improve property market efficiency. These collective measures are intended to support more stable and sustainable streams of equity funding to support new affordable projects and the ongoing operation of social and affordable housing assets. This goal will be greatly assisted by undertaking ancillary reforms which aid in the **normalisation of unimproved property prices.**

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[28] Crommelin, L., Troy, L., Martin, C. & Parkinson, S 2018, 'Technological disruption in private housing markets: the case of Airbnb', AHURI Final Report No. 305, AHURI, Melbourne. Website accessed 27-02-2020: https://www.ahuri.edu.au/research/final-reports/305, doi:10.18408/ahuri-7115201

[29] Government concessions/subsidies are critical to most of the proposed funding models. However, ISA learned from the discussion during the Community Housing Industry Council (CHIC) meeting (18 December 2019) that: 1. There is no new funding envelope for affordable housing; 2. There is a big shortfall/deficit in the current provision (a. that is barely maintaining the existing stock, let alone extending it; b. the NRAS incentives are currently running out in NSW; and c. demand is growing); 3. No forward commitment to new capital spending in government budgets; 4. Existing policy approaches to housing have no explicit consideration for family formation; 5. No coordination of strategies/policy approaches across government levels; 6. Duplication may be rife; and 7. No consistent set of policies to address the widening problem.

Overview of this discussion paper

The rest of the discussion paper is structured as follows.

Section 2 sets out the definitions of various types of social and affordable housing targeted towards community groups in need. These housing types are also identified in relation to the housing continuum by affordability. To keep descriptions of various types of subsidised housing succinct, unless otherwise stated, **we shall apply the term 'affordable housing' to represent all forms of subsided or assisted housing** in the remaining sections of this paper.

Section 3 identifies the existing supply and affordability gaps, and the current social housing waiting list in NSW.

Section 4 lists Federal, state (NSW) and local government policy and funding measures on affordable housing, along with expenditure data to improve our understanding of the current status of funding and what's budgeted for the future.

Section 5 provides analysis on adequacy and efficacy of current policies, areas of inefficiency and duplication, as well as inherent barriers to greater institutional investment. We also extend our coverage to broader issues with monetary policy.

Section 6 outlines alternative funding models developed to attract equity investment and boost the supply of affordable housing and close the supply gap. It also suggests structural reforms to macro and micro policy settings at the Federal and state level which would help to improve the efficiency of property markets across the nation and help to normalise unimproved property values over time. We also consider the challenges to affordable housing presented by the Covid-19 pandemic, and the need to contemplate affordable housing construction as part of any stimulatory measures to support economic recovery.

2. Housing definitions and concepts

This section outlines the definitions of various types of social and affordable housing targeted towards particular groups in our community. We shall also define their location on the housing continuum in relation to means of affordability.

2.1 Definitions

We first establish the definitions of a range of subsidised housing types dedicated to meeting the specific needs individuals and families.

Several types of subsidised housing are currently available to low-income and disadvantaged groups experiencing different levels of housing-stress. Suitable and affordable housing provided to individuals and families is an anchor point to enable them to better afford other essentials (food, clothing, transportation, medicine, etc) and to receive social services (education, crisis counselling, mental health, job-readiness etc) where needed on a sustainable basis. Such dwellings need to be suitably located within easy access to employment and services.

According to the NSW DCJ, here are the definitions of various types of subsidised housing available.

Table 1 – Definitions of housing types

Type	Description	Ownership and management
Social housing	Long term rental accommodation, subsidised by government, for people on a very low or low income, who meet the required eligibility criteria. It includes public, community and Aboriginal housing.	
- Public housing	Housing owned or leased by the NSW Land and Housing Corporation and managed by the Department, that is leased to members of the public that meet the Corporation's eligibility criteria. (NSW Housing Act 2001)	Housing owned or leased by the NSW Land and Housing Corporation and managed by the Department of Communities and Justice.
- Community housing	Housing provided by not-for-profit community housing organisations. Community housing offers secure, affordable rental housing for people on very low to moderate incomes who have various housing needs. There are several types of CHPss: - General Social Housing Providers – these offer long-term housing to clients; - Specialist Homelessness Services – these offer short to medium-term transitional housing to people who are homeless, in crisis or at risk of becoming homeless; and - Affordable Housing Services – some providers offer accommodation to people on low-to-moderate incomes.	Government, CHP and privately-owned properties, managed by non-government organisations.

- Aboriginal housing	Aside from public and community housing, Aboriginal (and Torres Strait Islander) people have access to housing provided by the Aboriginal Housing Office or by Aboriginal CHPs and Aboriginal Land Councils. The statutory body provides Aboriginal (and Torres Strait Islander) people with low cost and culturally sensitive housing that suits the living patterns and preferences of Aboriginal people.	NSW's Aboriginal community housing assets are owned by the AHO and managed by DCJ, CHPs and Aboriginal CHPs.
Affordable housing	Housing that is appropriate for the needs of a range of low to moderate income households and priced so that these households are also able to meet other basic living costs. This type of (government subsidised) housing is intended for people on a higher level of income, and households do not have to be eligible for social housing to apply for affordable housing. As a rule of thumb, housing is usually considered affordable if it costs less than 30 per cent of gross household income or less than 75 per cent of market rent. (NSW Affordable Housing Ministerial Guidelines 2018-19).	Owned and/or managed by registered CHPs.
Crisis accommodation	Emergency temporary accommodation for up to three months is available for people who are experiencing short-term housing crisis but not eligible for social housing. This type of housing is targeted towards people in the general community who are made homeless or facing hardship due to a crisis or emergency.	

Source: DCJ

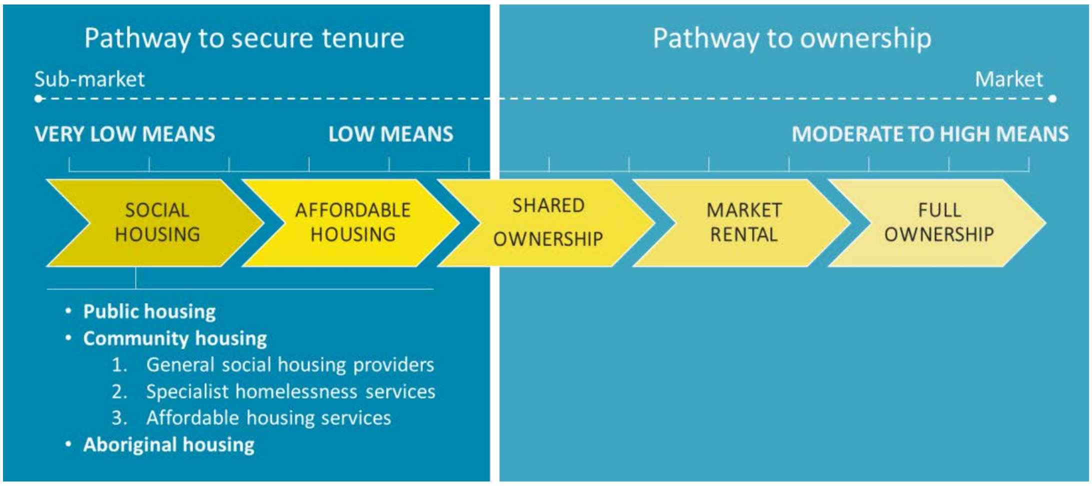
Note: Very low, low and moderate-income households are defined as: i) very low-income household earns less than 50 per cent of the relevant median household income for Sydney or rest of NSW; ii) low income household earns between 50 per cent and 80 per cent of the relevant median household income for Sydney or rest of NSW; iii) moderate income household earns between 80 per cent and 120 per cent of the relevant median household income for Sydney and NSW.

2.2 Pathways

The housing continuum outlines the spectrum of housing options available to people with limited means to achieve a secure rental tenancy and/or even dwelling ownership.[30] Several options are available to secure housing depending on income (Figure 3). The continuum begins with those individuals or families facing a crisis, or on very low incomes, experiencing housing stress that require sub-market rental accommodation. These options also provide certainty over tenure and in some instances, integrated services (for example mental health, job-readiness and building social capital skills etc). As we move up the income brackets, the capacity to afford better housing improves and residents eventually transition to full market rentals and/or market ownership.

[30] Means considers individual or households' wealth, income level and income generating ability in totality.

Figure 3 – The housing continuum

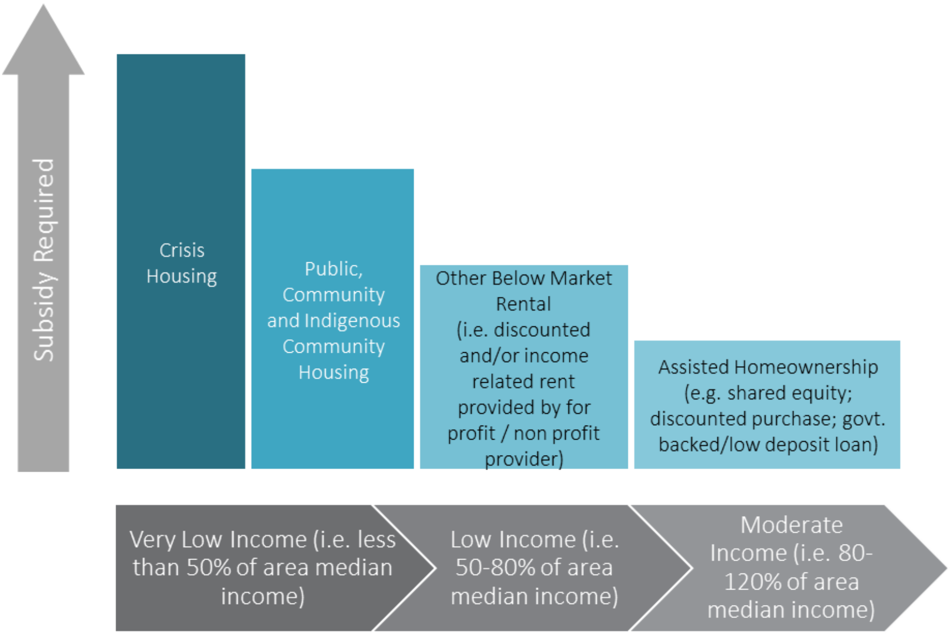


Source: AHURi, DCJ

Note: Crisis housing is usually placed at the low means end of the housing continuum. However, in many circumstances, people from various income levels seek access to such service.

To better understand the various types of affordable housing options, we revisit the definitions listed previously in Table 1. The range of housing models laid out according to the level of government subsidies required is compared in Figure 4. The line-up corresponds closely with the housing continuum as the level of subsidy declines with housing targeted at higher and higher income occupants.

Figure 4 –Affordable housing income and subsidy chart



Source: Gurran et al. (2018)

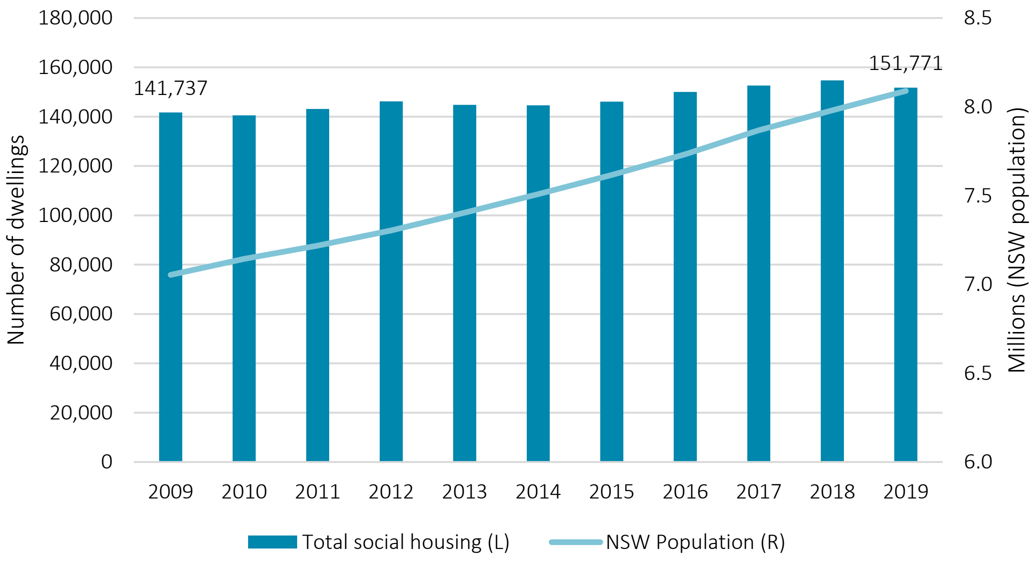
3. Housing shortages

This section examines the current level of housing stock, the funding gap and the shortfalls in NSW's affordable housing sector. This should aid in identifying the magnitude of current housing shortages and the quantities of new stock needed to keep up with rising demand. Different methodologies are employed in the estimation of housing shortfall. For example, relying on tenant income and housing costs, with housing stress identified when housing costs to income exceeds a defined ratio.

3.1 Social housing stock

Public housing constitutes most of the dwellings in the NSW social housing system. As of June 2019, the total number of public housing in NSW was 100,623, followed by community housing at 41,629 and the remainder (about 9,576) belongs to the Aboriginal Housing Office (AHO) and Indigenous Community Housing (ICH) providers.[31] As shown in Figure 5, the total housing stock has grown from just 10,034 units (of which 6,000 were added by GFC stimulus) over the past decade, while the NSW population has increased by over 1 million.

Figure 5 – Number of social housing dwellings in NSW compared to population



Source: Productivity Commission – Report on Government Services 2020 & ABS Cat.3101.0

Note: No data was available in the Productivity Commission datasheet for indigenous community housing for 2019.

[31] NSW DCJ 2019, *NSW Social Housing Residential Dwellings Dashboard*, Department of Communities and Justice. Website accessed 21/02/20: https://public.tableau.com/profile/facs.statistics#!/vizhome/Social_Housing_Residential_Dwellings/Dashboard.

Economic benefits of affordable housing construction

Affordable housing construction during periods of economic downturn such as the present Covid-19 pandemic can have a significant positive impact on regional output and employment. Such counter-cyclical investment creates additional demand for materials and labour, leading to increased economic activity as suppliers and contractors gear up to increase supply.

An example of government led affordable housing construction is the Western Australia (WA) Housing Authority shared equity Expression of Interest (EOI) procurement scheme for affordable housing back in 2011. An evaluation study on the EOI found wide ranging economic benefits of the procurement scheme. A study of the scheme found that based on the procurement expenditure of $293 million, the initial/direct construction activity induced was around $149 million of output, and the scheme supported a total of 1,491 jobs (directly and indirectly) and boosted indirectly the output of related supplier and services industries by $210 million. These values are shown in Tables 19 and 20 in ***Attachment A***.

Another notable study on the benefits of stimulatory spending on housing was the *Social Housing Initiative Review* by KPMG. The Social Housing Initiative (SHI) was a component of the Nation Building – Economic Stimulus Plan (NBESP) announced in the wake of the GFC.

The table below is sourced from the review and provides a summary of economic impacts of the SHI:

Economic Measures	Review Finding
Additional construction activity	Estimated to be $1.5 billion per annum on average in terms of the direct economic impact of the SHI.
Multiplier through the economy	For every $1 of construction activity, around $1.30 in total turnover (or an additional $0.30 in turnover) was generated in the economy.
Average annual value-added (gross domestic product (GDP))	$1.1 billion on average over the life of the SHI – approximately 0.1 per cent (10 basis points) of Australian GDP increase during the life of the SHI.
Employment	Construction industry increased by approximately 9,000 full time equivalent (FTE) positions (direct). The overall increase was approximately 14,000 FTE jobs (direct and indirect).

Source: KPMG (2012)

3.2 Community housing stock

There are currently 155 registered CHPs in NSW under the National Regulatory System for Community Housing (NRSCH).[32] The CHPs manage affordable housing properties under a wide variety of ownership structures. These fall into three broad categories:

[32] National Regulatory System for Community Housing 2019, *NRSCH Overview 2018-19 Part 1*, NRSCH National Office.

- Properties owned by Department of Communities and Justice (DCJ), managed by CHPs;
- Properties owned and managed by CHPs; and
- Properties owned by third parties and managed by CHPs.

Table 2 – Breakdown of ownership classification and tiers on properties managed by CHPs in NSW[33]

	LAHC owned / CHP managed (a)	CHP owned / CHP managed (b)	Third-party owned / CHP managed (c)
Tier 1	13,981	8,216	5,282
Tier 2	2,176	841	0
Tier 3	741	1	338
	14,000 (d)		
Total	**30,898**	**9,058**	**5,620**

Source: DCJ 'Regulatory Reform and Relationships in the Community Housing Provider Sector – NSW Options' and DCJ Future Directions Policy.

Note: (a) Providers retain all revenue streams (rent paid by tenants and CRA payments) typically with no specific subsidies payable from the NSW government. Recurrent maintenance obligations are retained by providers and major capital obligations retained by FACS. (b) Providers retain all revenue streams from tenants and all expense obligations are retained by providers. Government funding is dependent on the program under which property was obtained/developed. This arrangement typically applies to properties acquired/developed under the Social and Affordable Housing Fund (SAHF), Social Housing Initiative (SHI) and NRAS. (c) Providers generally retain revenue streams, with recurrent maintenance obligations typically sitting with providers and major maintenance obligations residing with third parties. Government subsidies are dependent on the program. This arrangement typically relates to properties under the Community Housing Leasing Program. (d) The Social Housing Management Transfer (SHMT) scheme transferred around 14,000 properties to CHP management. These properties are still owned by the LAHC.

3.3 Affordable housing gap

In this section, we provide a definition of the overall affordable housing gap in NSW by employing components based on affordability, subsidy and supply. According to the NSW DCJ, the stock of social housing (public, community and Aboriginal) as of June 2019 was 151,814.[34]

[33] Tier 1: the highest level of performance requirements and regulatory engagement, reflecting that these providers are involved in activities that necessitate management of a higher level of risk.

Tier 2: an intermediate level of performance requirements and regulatory engagement – reflecting that these providers are involved in activities that necessitate management of a level of risk lower than Tier 1 but greater than Tier 3.

Tier 3: a lower level of performance requirements and engagement – reflecting that these providers are involved in activities that necessitate management of a lower level of risk.

National Regulatory System Community Housing 2019, Registration page, 16 October 2019, Website accessed 16/10/2019: https://www.nrsch.gov.au/regulation_and_policy/registration.

[34] NSW DCJ 2019, *NSW Social Housing Residential Dwellings Dashboard*, Department of Communities and Justice. Website accessed 21/02/20: https://public.tableau.com/profile/facs.statistics#!/vizhome/Social_Housing_Residential_Dwellings/Dashboard.

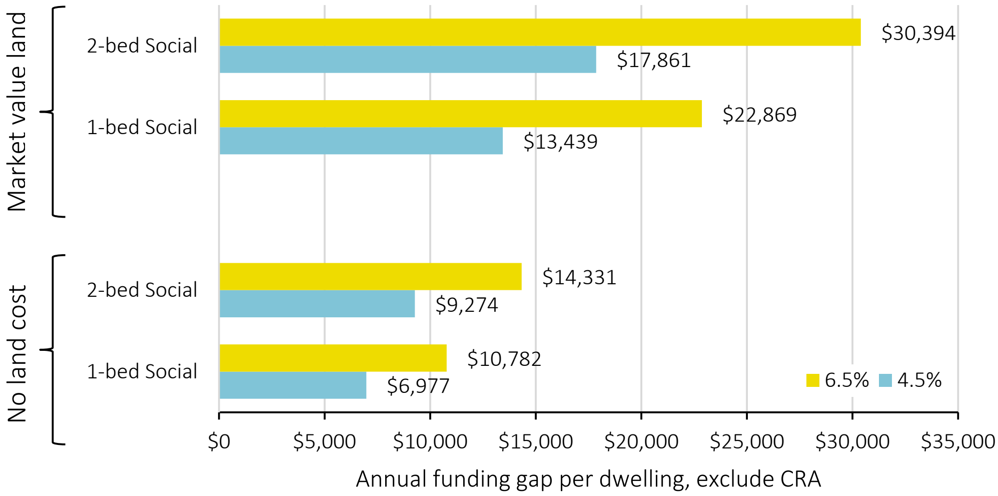
Affordability/funding gap

The affordability gap is defined in this paper as the difference between the market value or rent charged on a dwelling and the affordable price or rent that's paid by the low-income household. According to AHURI (2018), in the case for social housing, the affordability gap, or more precisely, the social housing funding gap, is the difference between the cost to supply, build, maintain and manage social housing and the rent paid by the social housing tenants inclusive of Commonwealth Rent Assist (CRA).[35] In the report, AHURI estimated a $13,000 per year national average funding gap for each social housing dwelling. The range of the funding gap for metropolitan Sydney varies between $10,000 to $35,000. While for regional and rural NSW, the range is much lower at between $5,253 to $10,000.

ISA modelling of the funding gap

ISA has also undertaken modelling to estimate the possible funding gaps that would enable a typical 100-unit build-to-rent (BtR) social housing development in NSW. The analysis identifies the approximate amount of government funding per dwelling required to achieve gross rate-of-return (RoR) targets. Our modelling supports the broad AHURI findings discussed immediately above based on fixed initial construction costs and a 15-year operating term.

Figure 6 – Estimated funding required to achieve gross nominal RoR targets (Sydney inner-city social rental)



Source: ISA modelling

Note: ISA modelling is based on a typical 100-unit BtR apartment development in inner-Sydney. No land cost means zero cost for land and no ongoing lease cost. Overall, the modelling assumed i) social rental costs charged at 25 per cent of household income, ii) for a 100-unit development, there are 60 two-bedroom units and 40 one-bedroom units, iii) a two year construction period, iv) $3,28 per unit maintenance costs v) $3,287 per unit rates & insurance, vi) 6 per cent vacancy rate, vii) 70 per cent equity and 30 per cent debt funding for development and 40 per cent debt amortisation, viii) cost of debt assumed at 2.75 per cent.

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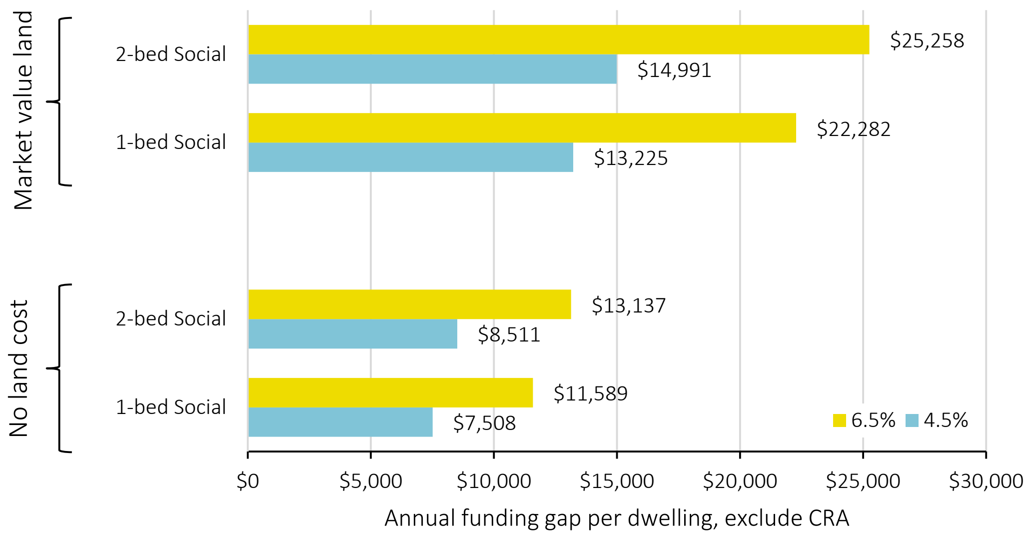
[35] Lawson, J., Pawson, H., Troy, L., van den Nouwelant, R. and Hamilton, C. 2018. 'Social housing as infrastructure: an investment pathway', AHURI Final Report No. 306, Australian Housing and Urban Research Institute Limited, Melbourne.

ISA modelling estimated that when land acquisition costs are factored in, the annual funding gap for a two-bedroom social (apartment) dwelling in inner-Sydney to be around $30,394 to achieve a gross RoR of 6.5 per cent (nominal), and around $17,861 to achieve a gross RoR of 4.5 per cent, see Figure 6. In all cases, the funding gap falls significantly if the state government is prepared to provide concessional land.

The modelling also revealed a lower level of funding required for social housing units located in the middle-to-outer suburbs of Sydney. We estimated that the annual funding gap for a two-bedroom social (townhouse) dwelling to be around $25,258 for a gross RoR of 6.5 per cent and around $14,991 for a gross RoR of 4.5 per cent, see Figure 7. Similarly, these funding gaps are reduced considerably when concessional land is provided.

Figure 7 – Estimated funding required to achieve gross nominal RoR targets (Sydney mid-outer social rental)



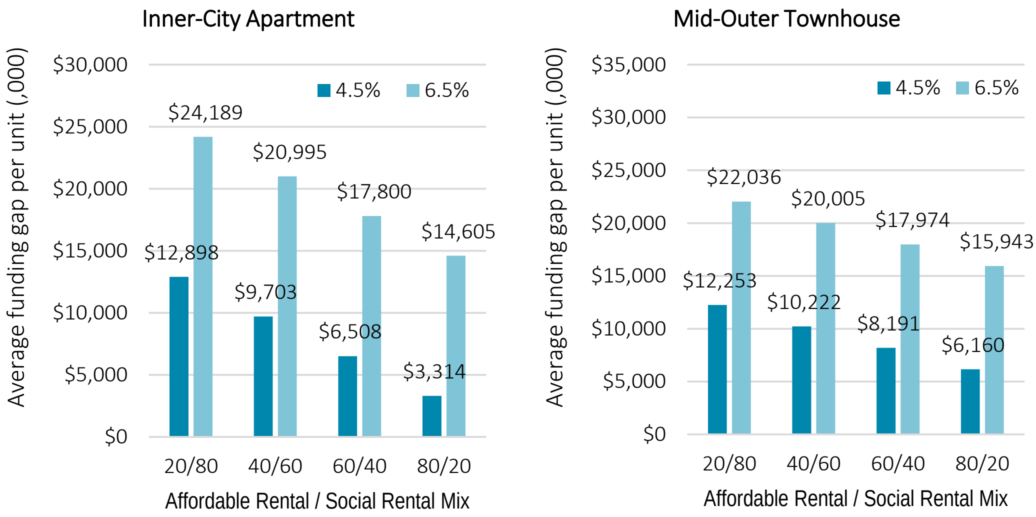
Source: ISA modelling

Note: ISA modelling is based on a typical 100-unit BtR townhouse development in mid-outer suburbs of Sydney. No land cost means zero cost for land and no ongoing lease cost. Overall, the modelling assumed i) social rental costs charged at 25 per cent of household income, ii) for a 100-unit development, there are 60 two-bedroom units and 40 one-bedroom units, iii) a two year construction period, iv) $3,28 per unit maintenance costs v) $3,287 per unit rates & insurance, vi) 6 per cent vacancy rate, vii) 70 per cent equity and 30 per cent debt funding for development and 40 per cent debt amortisation, viii) cost of debt assumed at 2.75 per cent.

Our modelling also suggested the funding gap for social housing units could be reduced significantly if a given housing development dedicates a portion of its dwellings to include affordable rentals (i.e. properties rented out to qualifying households at 75 per cent of market rates). For the inner-city mixed development scenario, with 40 per cent affordable rentals and 60 per cent social rentals, the annual funding gap to achieve gross RoR of 6.5 per cent is around $20,995 and this falls to $9,703 for a gross return of 4.5 per cent, see Figure 8. This scenario also assumed full land acquisition cost. The modelling shows if ongoing government funding is fixed, target returns could be met by altering the mix of affordable and social rentals. This can also be used to identify the optimal mix that requires the lowest amount of government funding.

Others have found that the funding gap may be reduced further via social housing cross-subsidised by market rate housing (provided by a CHPs with associated tax benefits). This has been found to be close to fully viable on a 4.5 per cent RoR basis.[36]

Figure 8 – Estimated average funding gap for mixed social and affordable development



Source: ISA Modelling

Note: Average funding gap per unit under a 100-unit mixed rental development. Affordable rent equates to about 75 per cent of market rent and higher than social rent. Land cost included in the modelling.

Supply gap

The supply gap refers to the current social and affordable housing need that is in addition to the 'met need' – households that are currently residing in social or affordable housing.[37] The estimates of the need for social and affordable housing are based on the analysis of households currently living under housing stress in the private rental market. These households are paying over 30 per cent of their income on rent. The housing needs also include the implied need from the homelessness population. The total social and affordable housing need for NSW is shown in Table 3.

In an alternative approach, a simulation was conducted by Rowley *et al.* for AHURI in 2017 which estimated the housing need in states and territories through the combination of several interacting models. The simulation determined housing need by several models including housing market, labour market earning and status, household formation and tenure choice. The simulation showed housing need in NSW was estimated to be 373,000 units in 2017 with the number rising to 678,000 units in 2025.[38] The model also estimated that there are around 140,000 households unable to access market housing in NSW and a further 233,000 households requiring rent assistance to alleviate a position of rental stress.

[36] See pp. 99-102 in https://cityfutures.be.unsw.edu.au/documents/558/LCOM_0000_Build_to_Rent_Report_WEB.pdf

[37] Troy, L., van den Nouwelant, R. & Randolph, B. 2019. 'Estimating need and costs of a social and affordable housing delivery', City Futures Research Centre, UNSW Built Environment, UNSW Sydney.

[38] Rowley, S., Leishman, C., Baker, E., Bentley, R. & Lester, L. 2017, 'Modelling housing need in Australia to 2025', AHURI Final Report No. 287, Australian Housing and Urban Research Institute Limited, Melbourne.

Table 3 – Need for social and affordable housing by state

State	Social housing shortfall 2019	Affordable housing shortfall 2019	Projected extra social housing needed by 2036	Projected affordable housing needed by 2036	Total needed by 2036
NSW	**137,100**	**79,400**	**76,100**	**24,100**	**316,700**
For comparison purposes, other states and territories have been included below					
ACT	3,100	2,400	5,200	1,000	11,700
NT	7,500	1,500	7,900	500	17,300
QLD	102,700	54,700	73,000	23,800	254,300
SA	33,100	10,300	16,300	2,300	61,800
Tas	11,100	3,300	3,000	500	18,000
Vic	103,900	42,700	62,400	16,700	225,600
WA	39,200	19,400	47,200	12,600	118,400
Total	437,700	213,700	291,100	81,500	1,023,800

Source: Troy et al. (2019)

Note: According to the study, housing need is split into two categories. The first category is households in the bottom income quintile ($400, $800 and $1,000 per week for singles, couples and families respectively) for Australia and requiring social housing, requiring a higher level of housing subsidy. The second category is households belonging to the second income quintile ($500, $1,250 and $1,750 per week for singles couples and families) and are experiencing housing stress, requiring a lower level of subsidy.

3.4 Social housing waiting list

The sufficiency of the current provision of social housing can also be assessed based on the number of applicants on the social housing waiting list.[39] The latest numbers for those waiting for social housing are set out below. For NSW there were 51,014 applicants as of June 2019 (Figure 9) down from 57,791 in June 2014. Of these applicants, 4,484 are classified as 'greatest needs' or priority applicants who are either homeless or at risk of homelessness.[40] In terms of the rest of Australia, Victoria has the highest number of applicants on the social housing waiting list (52,509), followed by Queensland (42,501), South Australia (35,738) and WA (15,458). The

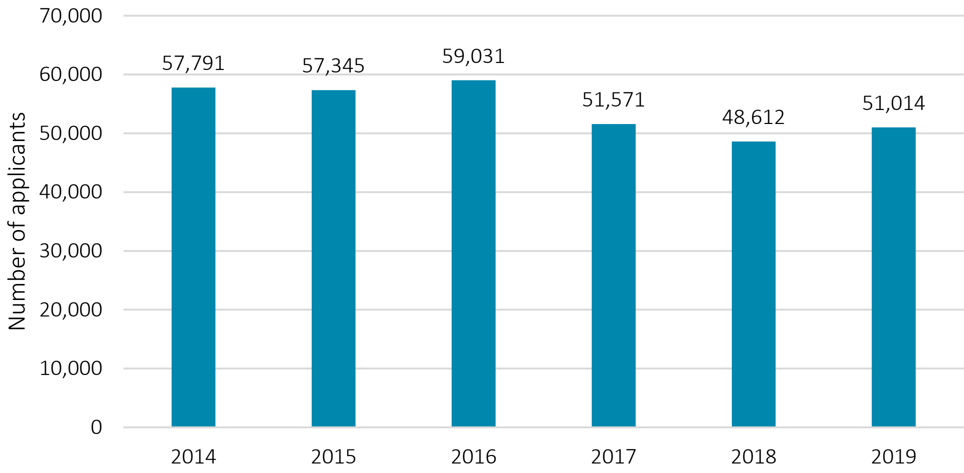
[39] The number of applicants on the social housing waiting list depends on eligibility criteria established by the government and can change significantly as the criteria changes. Hence this is not an ideal proxy for the level of social housing need. We welcome recommendations on better representative indicators on measuring the need for social housing.

[40] Applicants with the 'greatest needs' may also have health conditions that were exacerbated by current living conditions. Latest applicant numbers on the social housing waiting list sourced from NSW DCJ housing assistance expected waiting times. Website accessed 3/02/2020: https://www.facs.nsw.gov.au/housing/help/applying-assistance/expected-waiting-times.

total number of persons on the social housing waiting list in Australia was 207,899 by 30 June 2019.[41]

It should be acknowledged that social housing waiting lists are a poor proxy for need and that state governments can remove individuals by setting stricter eligibility criteria, failing to increase income thresholds in line with inflation or excluding households for perceived offences.

Figure 9 – NSW social housing waiting list



Source: Productivity Commission – Report on Government Services 2020, NSW DCJ

Homelessness on the rise

According to statistics published by the latest Productivity Commission Report on Government Services 2020, the rate of homelessness in NSW has risen from 39.7 per 10,000 of the population in 2011 to 50.4 per 10,000. In particular, the rate for homeless people living in improvised dwellings, tents or sleeping out has risen from 2.8 to 3.5. Please refer to **Attachment E** for the complete table.

3.5 Measuring the loss to community

Inadequate and insecure housing negatively impacts on families' health and wellbeing and can have short and long-term economic consequences.

Insecure housing strains family relationships and leads to poor educational outcomes for children. This adversely impacts on their future earning potential, leads to reduced social contribution and greatly increases the likelihood of welfare dependency. The negative impact on human capital from a lack of secure housing is significant and ultimately leads to lower productivity potential for the individual.

Inadequate provision of affordable housing also forces households to relocate out to the suburban fringes in search for low rent accommodation. This lengthens commute times to

[41] Productivity Commission 2020, *Report on Government Services 2020*, Website accessed 30/01/2020: https://www.pc.gov.au/research/ongoing/report-on-government-services/2020/housing-and-homelessness/housing.

employment locations and results in a poorer job matching between workplace and skills. **Attachment B** presents research from Maclennan *et al.* (2019), which explores the loss in productivity from the human capital perspective and shows how productivity benefits from 'Better Housing Outcomes' (BHO) can be measured. Achieving BHO not only examines productivity benefits of households residing in localities close to employment, but also how reducing housing costs can have a positive impact on wellbeing and education outcomes. **Attachment C** present findings from Nygaard (2019), which quantifies the health and wellbeing savings on the wider society and to the individual by transitioning from homeless to secure housing. These studies present the economic and intergenerational cost of housing inadequacies and the consequences of policy failure or inaction.

4. Existing funding and policy approaches

In this section, we present a range of measures currently in place at the Federal level, NSW state level and local level that are aimed towards countering the existing affordable housing gap. We begin with an overview of NSW policies and total funding sources. We then provide a detailed breakdown of policy and funding at each level of government. We end with a look at some indirect policies that may be contributing positively or negatively towards bridging the housing gap.

The current funding allocation for NSW DCJ and related agencies that handle housing provisions is summarised in Figure 10. In addition to rental revenues, the DCJ receives most of its funding from the Commonwealth under the National Housing and Homelessness Agreement (NHHA) to the amount of $485 million. State funding for DCJ stands at $382 million while investment revenues from the Social and Affordable Housing Fund (SAHF) came in at $21 million. There are other policies that provide funding directly to tenants and investors of affordable housing, these are listed under 'Other schemes'.

Figure 10 – Funding measures for NSW

NSW DCJ Funding sources	Level	2019-20
NHHA	Commonwealth	$485 million
NPARIH	Commonwealth	$30 million
State consolidated funding	State	$382 million
LAHC (rental income)	State	$740 million
AHO (rental income)	State	$56 million
SAHF	State	$21 million
Other	State	$83 million
Total		**$1,797 million**

Other schemes
CRA (2018-19) $1.42 billion (NSW)
NRAS (June 2019) 447 incentives outstanding (NSW)
NHFIC (June 2019) $308 million (national)

Local council schemes
$550 million

Source: NSW DCJ, NHFIC, Productivity Commission, DSS

4.1 Federal level

In the following section, we will explore the major Federal level policies for housing and homelessness. We outline aggregate commitments, provide a detailed breakdown of their funding provisions and identify other indirect schemes that may influence housing gaps.

There are several Federal level policies and agencies that provide funding and investment to states and territories. These include the NHHA, which was established to replace the National Affordable Housing Agreement (NAHA). It combines funding allocated under National Affordable Housing Specific Purpose Payment (NAHSPP) and the National Partnership Agreement on Homelessness (NPAH). The other major Federal initiative was the establishment of National Housing Finance and Investment Corporation (NHFIC), which operates the National Housing Infrastructure Facility (NHIF) and Affordable Housing Bond Aggregator (AHBA). Additional Federal level measures that support rental affordability include the Commonwealth Rent Assist (CRA) and the National Rental Affordability Scheme (NRAS)[42], the latter was discontinued under the Abbott government in 2014.

The major Federal level policy-set and their total national commitments are shown in Table 4.

Table 4 – Aggregated federal expenditure (nationally)

National Housing and Homelessness Agreement (NHHA)	Commonwealth Rent Assist (CRA)	National Rental Affordability Scheme (NRAS)
$1.56 billion[1]	$4.44 billion[2]	34,689 incentives[3]

Source: NHHA, NHFIC Annual Report 2018-19, Productivity Commission Report on Government Services 2019, Department of Social Services

Note: 1. Fiscal year 2019-20, 2. Total government expenditure for fiscal year 2017-18, 3. Total number of incentives paid for fiscal year 2018-19.

In subsections below, we describe and present each of the major national policies and the breakdown of their funding commitments.

4.1.1 National Housing and Homelessness Agreement (NHHA)

The NHHA is a joint initiative by the Commonwealth and state governments to improve the provision of housing across the housing spectrum. The initiative also seeks to jointly address the growing problems of homelessness or those at risk of becoming homeless. The latest agreement replaces NAHA and the NPAH. The Commonwealth and the states are required under this agreement to jointly improve housing and homelessness outcomes and are assessed against the six outcomes as agreed to by the Commonwealth, state and territory governments.[43]

Under NHHA, the states are required to allocate funding from the Commonwealth to housing and homelessness services. For the budget year of 2019-20, the total Commonwealth contribution stands at $1.6 billion (with state and territory governments contributing an additional $125 million). As listed below, Table 5 shows the breakdown of funding allocated towards various programs and services from the Federal level.

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[42] NRAS was discontinued in 2014, however there are still 1,850 incentives yet to be delivered, which continue to support existing pool of NRAS dwellings into 2020.

[43] 1. People who are homeless or at risk of homelessness can achieve sustainable housing and social inclusion; 2. People are able to rent housing that meets their needs; 3. People can purchase affordable housing; 4. People have access to housing through an efficient and responsive housing market; 5. Indigenous people have the same housing opportunities (in relation to homelessness services, housing rental, housing purchase and access to housing through an efficient and responsive housing market) as other Australians; and 6. Indigenous people have improved housing amenity and reduced overcrowding, particularly in remote areas and discrete communities. Australian Institute of Health and Welfare 2014, *Housing assistance in Australia 2014*, The Australian Government, Website accessed 21/11/19: https://www.aihw.gov.au/getmedia/26e52b0d-d318-4bf7-9ddf-7d8e86f51935/17154-18feb2015.pdf.aspx.

Table 5 – NHHA Estimated financial contributions

($ million)	2018-19	2019-20	2020-21	2021-22	2022-23	Total
Estimated total budget (1)*	1,656.9	1,689.9	1,725.1	1,684.3	1,709.6	8,465.8
Estimated National payment (2)						
General	1,379.1	1,398.4	1,419.4	1,440.7	1,462.3	7,099.8
Homelessness	116.6	118.2	120.0	121.8	123.6	600.3
General (Social and Community Services)**	35.7	41.5	47.6	tbd	tbd	124.8
Homelessness (Social and Community Services)	4.5	6.8	9.1	tbd	tbd	20.3
Total Commonwealth contribution	1,535.8	**1,564.9**	1,596.0	1,562.5	1,585.9	7,845.2
Balance of non-Commonwealth contributions# (3) = (1) – (2)	121.1	**125.0**	129.1	121.8	123.6	620.6

Source: National Housing and Homelessness Agreement

*Note: * This is the total Commonwealth contribution plus the state matched funding required under sub clause 17(e). ** SACS funding beyond 2021-22 is subject to a future government decision given that Commonwealth funding under the National Partnership Agreement on Pay Equity for the Social and Community Services Sector is terminating. # This is the state matched funding required under sub clause 17(e).*

The Commonwealth's expenditure on affordable housing is also captured in the Federal budget papers as shown in Table 6. In addition to the NHHA, it also shows the total National Partnership Payments. In total, the Commonwealth in budget year 2019-20 committed $1.7 billion to support affordable housing and homelessness services, of which $484 million are allocated to NSW.

Table 6 – Payments to support state affordable housing services

($ million)	2018-19	2019-20	2020-21	2021-22	2022-23
National Housing and Homelessness Agreement	1,535.8	1,564.9	1,597.6	1,565.6	1,590.6
of which received by NSW	*476.4*	*484.2*	*493.1*	*493.5*	*501.6*
National Partnership payments					
National Regulatory System for Community Housing	0.8	0.3	-	-	-
Northern Territory remote Aboriginal investment					
Remote Australia strategies components	27.3	3.5	3.7	3.7	-
Remote Housing	268.5	110.0	110.0	110.0	110.0
Social Impact Investments					
Vulnerable priority groups	-	0.5	0.5	0.5	0.5
Youth at risk of homelessness	-	0.5	0.5	0.5	0.5
Total National Partnership payments	296.6	114.9	114.7	114.8	111.1
Total	1,832.4	1,679.8	1,712.3	1,680.3	1,701.7

Source: 2019-20 Budget Paper No.3

The breakdown of the $484 million allocation to NSW is shown in Table 7. In 2019-20, $441 million was allocated to general housing and services while $31 million was allocated to the state for homelessness services. Aside from allocating funds received from the Commonwealth, the states were also required to provide matching contributions with respect of Commonwealth's homelessness funding.

Table 7 – NHHA state allocations (estimates)

($ million)		2018-19	2019-20	2020-21	2021-22	2022-23	Total
Estimated National payment							
General							
	NSW	441.1	447.5	454.5	461.5	468.4	**2,273.0**
General (SACS)*							
	NSW	4.7	5.5	6.3	tbd	tbd	**16.5**
Homelessness							
	NSW	30.4	30.9	31.3	31.8	32.3	**156.7**
Homelessness (SACS)*							
	NSW	0.6	0.9	1.2	tbd	tbd	**2.6**

Source: National Housing and Homelessness Agreement

*Note: All numbers are estimates provided by NHHA. Modified to show NSW only. *SACS funding beyond 2021-22 is subject to a future government decision given that Commonwealth funding under the National Partnership Agreement on Pay Equity for the Social and Community Services Sector is terminating.*

4.1.2 National Housing Finance and Infrastructure Corporation (NHFIC)

The NHFIC was established by the Commonwealth as an agency that offers loans, grants and investments to encourage the construction of affordable housing and related infrastructures.

The investment corporation oversees NHIF, which provides grants and loans to Commonwealth and state initiatives in the provision of housing outcomes and the building of critical infrastructure to support the supply of new housing. Up to $1 billion in funding was made available from the NHIF, of which $600 million is concessional loans, $225 million is equity investments, and $175 million is grants.[44]

NHFIC also operates the AHBA, which aims to provide low-cost, long-term loans to finance community housing projects through bond issuance.[45] In March 2019, the NHFIC issued $315 million in social bonds with an interest rate of 48 basis points above government bond yields. These low-cost loans offer interest rate and term (tenure) advantages for CHPs compared with typical bank loans. The issuance drew both local and offshore investors and was four times oversubscribed. Major investors include **Cbus**, **UniSuper**, **CareSuper** (via UBS), Blackrock Investment Management, AIA, QIC and QBE Insurance. Investor take-up of the bonds was strong. Investors were receptive to the quality (government-backed AAA-rated) and anticipate category will grow to become a "significant asset class of its own".[46] In November 2019, there was a second issuance ($315 million worth of NHFIC bonds) to help finance seven CHPs building over 2000 properties across Australia. The issuance was again four times

[44] The Treasury 2019, *Housing Policy – National Housing Finance and Investment Corporation*, Website accessed: 15/08/19: https://treasury.gov.au/housing-policy

[45] National Housing Finance and Investment Corporation 2019, *Annual Report 2018-19*, Website accessed: 20/11/19: https://www.nhfic.gov.au/media/1148/nhfic-annual-report-2018_19.pdf

[46] Bleby, M., 'In-demand affordable housing bonds a future new asset class: NHFIC', *The Australian Financial Review*, 29 March 2019.

oversubscribed and enabled a low fixed rate loan of 2.07 per cent over 10.5 years.[47] Super funds such as Cbus Super, CareSuper and UniSuper invested in the second issuance, with Cbus acting again as the cornerstone investor. Kristian Fok, Cbus Super CIO said the fund was "pleased to invest in NHFIC bonds that meet our investment risk-return criteria and fund new housing construction for Australians in need".[48]

Table 8 – Quick facts on the NHFIC 2018-19

Line of credit from the Commonwealth	$ 1.0 billion
Total loan commitments 2018-19	$ 472 million
Loans settled before 30 June 2019	$ 308 million
Social bond issued*	$ 315 million

Source: NHFIC Annual Report 2018-19.
*Note: *A second round ($315 million) of social bond was issued in November 2019.*

Aside from supporting affordable housing financing through investing in NHFIC bonds, the not-for-profit superannuation sector has also invested directly in this sector to provide housing for essential workers in our community and those in housing stress.[49]

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[47] Cranston, M., 'Cbus, UniSuper in $315m bond raise for new housing', *The Australian Financial Review*, 20 November 2019, Website accessed 24/4/2020: https://www.afr.com/politics/federal/cbus-unisuper-in-315m-bond-raise-for-new-housing-20191120-p53cbb

[48] NHFIC 2019, *NHFIC Bonds Exceed $600M with Second Bond Issuance*, NHFIC Media Release, 20 November 2019, Website accessed 24/4/2020: https://www.nhfic.gov.au/media-resources/media-releases/nhfic-bonds-exceed-600m-with-second-bond-issuance/

[49] AustralianSuper has acquired a 25 per cent stake in affordable housing developer Assembly Communities. The developer offers homes that occupants can rent for up to five years before buying and includes provisions for essential workers' housing. This was the first investment in scalable housing platforms made by AustralianSuper, and it expects to invest in excess of $100 million per year in a pipeline of homes from the developer. Its first investment with Assemble will be a 198-unit development in Melbourne's north-western suburb of Kensington.

Bleby, M., 'AustralianSuper takes 25pc stake in build-to-rent platform', *The Australian Financial Review*, 11 June 2020.

First State Super announced in July that the fund will double its investment in key-worker affordable housing from $200 million to $400 million in 2020. The fund has already invested $200 million in affordable housing developments to support workers such as nurses, teachers, emergency services personnel, aged and disability support workers, childcare employees and other workers in related industries. Many of these workers are in the frontline battle against Covid-19. The current portfolio of affordable housing sites includes Epping, Waterloo, Hurstville and Northmead in Sydney, and Moonee Ponds in Melbourne. It has also invested in a BtR affordable housing project in Miranda NSW, with construction beginning in 2020.

First State Super 2020, 'Aware Super to take leading role supporting Australia's economic recovery', Media Release, 15 July 2020, Website accessed: 28/07/2020, URL: https://firststatesuper.com.au/content/dam/ftc/digital/pdfs/about/media/2019/2019.07.08%20%20Affordable%20Housing%20-%20First%20State%20Super%20leads%20in%20Affordable%20Housing.pdf,

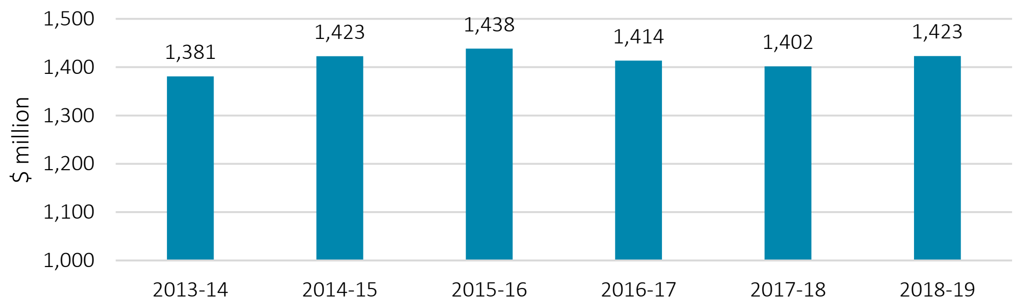
First State Super 2019, 'Investment in Affordable Housing Briefing', Briefing, 6 December 2019

HESTA has invested $20 million in a partnership with community housing group Nightingale Housing and not-for-profit Social Ventures Australia (SVA) to develop 185 apartments in Brunswick (inner-north Melbourne). About 20 per cent of the apartment units will be rented to key service workers such as nurses and workers in the aged care and not-for-profit sectors. Another 20 per cent of the units will be available as affordable rentals to eligible tenants. The remainder will be market sales. The investment was made through HESTA's $70m Social Impact Investment Trust (SIIT), which is managed by SVA to provide a risk-adjusted market return as well as to provide a social impact.

4.1.3 Commonwealth Rent Assist (CRA)

The CRA provides financial assistance to eligible individuals who rent in the private market or community housing. To qualify for the program a person must rely on a social security income support payment or Family Tax Benefit A also pay a minimum amount of rent. Over 40 per cent of individuals in the private rental market receive CRA payments. In 2018-19, total CRA payments for NSW were approximately $1.4 billion (see Figure 11).[50] The CRA has had a major impact on reducing the effects of rental stress on individuals.

Figure 11 – Total CRA payments for NSW



Source: Productivity Commission Report on Government Services 2020

It is estimated that CRA has led to a 23 percentage point reduction in the number of low-income recipients in housing stress, see Table 9.[51]

Table 9 - Percentage of CRA income recipients in rental stress before and after CRA

Outcome performance measure	2015–16	2016–17	2017–18
Before	68.2%	68.5%	68.3%
After	41.2%	41.6%	40.3%

Source: Department of Social Services Annual Report 2017-18

Despite making a valuable contribution to affordability for private renters, there are two major concerns with the CRA arrangement:

HESTA 2019, 'HESTA invests in scalable model to help address housing affordability', Media Release, 08 August 2019, Website accessed: 7/08/2020. URL: https://www.hesta.com.au/about-us/media-centre/HESTA-invests-in-scalable-model-to-help-address-housing-affordability.html

NGS Super maintains a $500,000 exposure to social benefit bonds (the Aspire SIB), which invests in reducing homelessness in South Australia. The bonds fund the Aspire Program, which is delivered by the Hutt Street Centre, an Adelaide based homelessness services specialist, in partnership with CHPs including Common Ground Adelaide and Unity Housing.

NGS Super 2020, 'Solid investment returns plus social benefits – it's a win-win', Articles – Sustainability, 16 Jan 2020. Website accessed: 4/08/2020. URL: https://www.ngssuper.com.au/articles/sustainability/solid-investment-returns-plus-social-benefits

[50] National Commission of Audit 2014, *Towards Responsible Government – Phase One, February 2014*, Website accessed: 14/08/19: https://www.aihw.gov.au/getmedia/7a75968e-5d4b-4aa9-b0d3-b34e0f771f12/17154.pdf.aspx?inline=true

[51] Department of Social Services 2018, *Annual Report 2017-18*, Canberra.

- Current increases in CRA (indexed to CPI) are not keeping up with rises in rents; and
- Despite wide variations in rents across the country, the entitlements standards (e.g. maximum level of assistance) are uniform, which means it is 'weakly responsive to regional variations in the amounts of rent being paid'.[52]

4.1.4 National Rental Affordability Scheme (NRAS)

The NRAS provided subsidies to housing providers to deliver affordable rental dwellings with rents at least 20 per cent below market rates for 10 years. The program supported eligible medium to low income earners unable to afford market prices. The incentives, of approximately $10,000 per dwelling (indexed) every year for 10 years, were given as a refundable tax offset or direct payment for the Commonwealth portion. The state component was given to private NRAS participants and as either cash or upfront capital grants to CHPs. The state and Commonwealth governments both contributed to the incentive, with state governments being required to provide 25 per cent of total.

The program was discontinued in May 2014 by the Abbott Government.

Accumulated NRAS exits by 2026 will be 6,549 in NSW and 36,721 nation-wide according to Department of Social Services (2018).

CHIA has suggested maintaining a reduced rate of NRAS for another few years to encourage investors to maintain stocks of affordable dwellings as well as allowing an 'availability subsidy' for CHPs to offer rental subsidies for cohorts such as aged renters or family violence survivors.[53]

In its 2017-18 Annual Report, the Federal Department of Social Services found as of April 2017, NRAS has reduced the proportion of client households in rental stress by 22 per cent.

Table 10 - Percentage of client households in rental stress before and after NRAS

Outcome performance measure	2016–17 NRAS year	2015–16 NRAS year
Before	84.2%	86.7%
After	61.6%	63.5%

Source: Department of Social Services Annual Report 2017-18

4.1.5 Indirect approaches

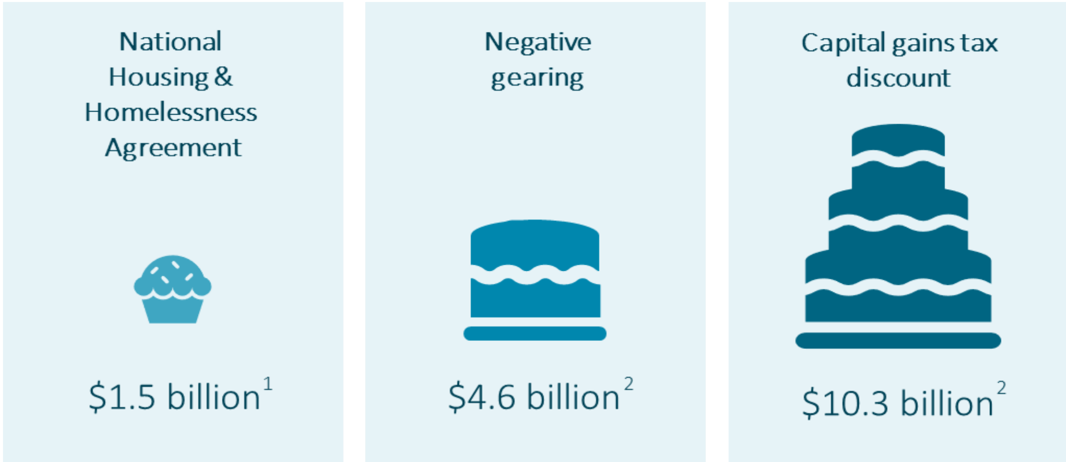
Other budget fiscal policies (subsidies, expenditures, credits and concessions) which were designed to foster broader investment and savings goals also impact affordable housing. These have increasingly become popular ways by which Australian governments provide support to residential property ownership often in the guise of supporting the construction of residential housing. These measures directly prime property market prices and so may worsen housing affordability. For example at the Federal level, the combined annual cost of negative gearing

[52] King, A. & Melhuish, T. 2003, 'The regional impact of Commonwealth Rent Assist', AHURI Positioning Paper No. 57, AHURI, Melbourne. Website accessed 19-02-20: https://www.ahuri.edu.au/__data/assets/pdf_file/0014/2813/AHURI_Positioning_Paper_No57_The_regional_impact_of_Commonwealth_Rent_Assistance.pdf

[53] Community Housing Industry Association (CHIA) 2018, "Live Post NRAS", Website accessed 13/08/19: https://www.communityhousing.com.au/post-nras/

and capital gains tax discount at $12 billion nationally.[54] This according to Troy *et al.* (2019),is far higher than the annual cost of building over 1 million social and affordable housing nationwide (by 2036) – to meet the estimated housing shortage, would be $8.6 billion per year.[55] Such a comparison shows bridging the housing gap can be achieved if the Australian government reprioritises its policy targets (Figure 12).

Figure 12 – Federal level national expenditure comparison



Source: NHHA, Per Capita

Note: 1. Commonwealth contribution for fiscal year 2018. 2.Estimates by Per Capita for Anglicare Australia (2018).

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[54] Other studies such as 'The Cost of Privilege – A Research Paper by Per Capita for Anglicare Australia' estimates the combined cost of negative gearing and capital gains tax discount to be around $14.9 billion a year.

[55] Based on the 'operating subsidy' funding model and allowing for both social and affordable housing across the whole of NSW – figures drawn from Tables 3 and 8 in Troy et al (2019). Aside from building affordable housing, it is also important to acknowledge that there are other approaches such as upfront grants, land provision, inclusionary zoning and indirect measures that can also assist with closing the housing gap.

The 'operating subsidy' model outlined in Troy *et al*. (2019) for social and affordable housing provision assumed that the subsidies would be paid annually over 10-years (out of 20-years delivery program), and the development would be financed wholly through NHFIC loans at an interest rate of 5 per cent (with 1.5 per cent discount). The model sought to identify a 'neutral cash flow balance' in the project's net present-value NPV and therefore was not a 'for-profit' model (in comparison with ISA modelling directly below which assumed a positive rates-of-return).

In contrast, the funding gap modelling undertaken by ISA (see Section 3.3) assumed a 70/30 equity/debt mix with targeted rate-of-return (RoR). The interest rate on loans was assumed to be 4 per cent less 1.25 per cent discount, with 40 per cent of the loan amortised during the period of development and operation. The for-profit operation would run for 15 years and the model assumed the development will be purchased by another buyer at market price at the end of 15 years.

Negative gearing

Negative gearing allows losses incurred on an income producing asset to be offset against all of a taxpayer's taxable income, including income not related to that asset. Negative gearing encourages taxpayers to employ high levels of leverage (which reduces the amount of capital required by investors and maximises tax losses). Investors take advantage of the arrangement and through the use of leverage, distort the property markets for owner-occupiers. This also impacts the yield on residential property which has discouraged institutional investors playing a greater role in the sector over time. These factors have exacerbated housing affordability and household debt levels associated with the domestic economy.

The cost of the negative gearing concession on residential property to the Federal budget is estimated at approximately $4.6 billion per year.

Capital gains tax discount

Capital gains tax (CGT) on property is applied to only 50 per cent of the appreciation (a discount of 50 per cent) if an asset is held for 12 months or more. The discount aims to ensure that taxpayers are only taxed on the real value of capital gains. This tax distortion encourages speculation on land. Acting in tandem with the negative gearing concession, it encourages investors to allocate too heavily to property and take on too much debt. This also distorts property markets by driving up prices and driving down yield over time. The discount also reduces the progressivity of the tax system as capital gains are not distributed evenly compared to other forms of income.[56]

The cost of the discount on capital gains for residential property to the Federal budget is estimated at approximately $10.3 billion per year.

4.2 State level

In this subsection, we will explore the funding allocated by the NSW state government to its departments and related agencies, breaking down departmental funding and expenditures. Also, we provide a brief overview of direct and indirect policies in place to address the housing gap.

On a state level in NSW, the DCJ allocates Federal and state sourced funding to support various housing programs. Agencies such as the LAHC and AHO are also directly involved in the provision and management of social housing. Collectively, the state level agencies formulate and carry out the policy set shown in Table 11. These are direct policies aiming to increase the stock of social and affordable housing through partnerships with non-profit CHPs.

[56] Daley, J. & Wood, D., 2016, 'Hot property – Negative gearing and capital gains tax reform', Grattan Institute, Melbourne. Website accessed 23/01/2019: https://grattan.edu.au/report/hot-property/.

Table 11 – State level agencies and policy set

Departments and agencies overseeing housing policy	Direct policy set
Department of Communities and Justice (DCJ) Department of Planning, Industry and Environment (DPIE) - Land and Housing Corporation (LAHC) - Aboriginal Housing Office (AHO) - Landcom	Communities Plus Social and Affordable Housing Fund (SAHF) Community Housing Innovation Fund (CHIF) Social Housing Management Transfer (SHMT) Community housing leasing program National Rental Affordability Scheme (NRAS) SEPP (Housing for Seniors or People with a Disability) Affordable Rental Housing (SEPP) SEPP 70 Affordable Housing Revised Schemes

Source: DCJ

The aggregate expenditures for the major state government departments and agencies are shown in Table 12.

Table 12 – Aggregated state level expenditure 2019-20

Department of Communities and Justice (DCJ)	Land and Housing Corporation (LAHC)	Aboriginal Housing Office (AHO)
$967 million	$1,401 million	$123 million

Source: DCJ
Note: Approximately one-third of LAHC's expenditures are categorised as depreciation expense ($523 million).

In the subsection below, we describe and present major departmental funding and expenditures for 2019-20.

4.2.1 State level expenditure and funding for housing services

The provision and management of affordable housing and homelessness programs in NSW fall under the DCJ, along with the AHO and LAHC. [57] The key functions of the DCJ in relation to assisted housing includes negotiating funding from the Commonwealth under the NHHA, and commissioning and managing the delivery social housing, while crisis, transitional and affordable housing are delivered by other providers on behalf of the DCJ. For the budget year 2019-20, the DCJ received $485 million from the Commonwealth as part of the NHHA and $30 million under the NPARIH[58]. The department also received funding of $382 million from State Consolidated Funding as shown in Table 13. The DCJ also provided funding to the AHO and

[57] The Aboriginal Housing Office (AHO) and Land and Housing Corporation (LAHC) fall under the NSW Department of Planning, Infrastructure and Environment (DPIE).

[58] The National Partnership Agreement on Remote Indigenous Housing (NPARIH).

LAHC in the sum of $55 million and $89 million respectively, while rental income came in at $56 million and $740 million respectively. Detailed breakdowns of funding for AHO and LAHC can be found in Attachment D.

Table 13 – Total funding for the NSW Department of Communities and Justice and related agencies (homelessness and social housing)

($ million)	2019-20
Commonwealth	515
NHHA – Commonwealth	485
NPARIH – Commonwealth	30
State consolidated funding (to DCJ)	382
State Consolidated Funding (includes $103m for tenancy management of LAHC properties – from LAHC)	
LAHC – rental income	740
AHO – rental income	56
Other sources	104
SAHF Revenue – received from Crown (i.e. State funds)	21
HPAF	8
Rental Bond Board	3
Other sources	6
Grants from other government agencies & SPP payments	16
Recovery water charges	40
Interest income	3
Management fee revenues	7
Total Funding	1,797

Source: DCJ

Note: Total expenditure excludes subsidies for first home buyers.

Expenditures by DCJ, LAHC and AHO budgeted for 2019-20 were $967 million, $1,401 million and $123 million respectively, see Table 14. In particular, $210 million was budgeted for ‘Specialist homelessness services’, $38 million for ‘Homelessness strategy & temporary accommodation’ and $49 million for ‘Youth homelessness, crisis accommodation & crisis and prevention services’. Tenancy management services (under DCJ) was another major item at $103 million.

Table 14 – Total expenditure by the NSW Department of Communities and Justice and related agencies (homelessness and social housing)

($ million)	2019-20
Department of Communities and Justice	**967**
Specialist Homelessness Services (majority support programs through contracts with NGOs)	210
Homelessness Strategy (Yr 2) & Temporary accommodation	38
Youth Homelessness, Crisis Accommodation & Crisis and Prevention Services	49
LAHC support for the government owned social housing properties	50
Public Housing lease subsidies to LAHC – (for headlease)	41
AHO support – management of 6,000 AHO housing properties	35
NPARIH NP to AHO (new supply and repairs and management of AHO properties)	25
Community Housing Lease Subsidies	84
Future Directions services improvement programs – (incl Private Rental Subsidies, Personnel support plans, Opportunity Pathways, Career Pathways, Scholarship and Mentoring & Tenancy Bonds)	33
Support for range of social housing sector entities (including CHPs and peak organisations)	25
Social and Affordable Housing Fund (payments for SAHF delivery)	19
Private Market Assistance (Rent Choice, PRA and HOMES under Future Directions)	21
Tenancy management services	103
Range of small grants, operational district management and corporate costs (accommodation, IT, depreciation etc)	234
Land and Housing Corporation (LAHC)	**1,401**
Recurrent grants (other housing grants)	3
Personnel services/employee related	78
Depreciation expense	523
Repairs and maintenance	272
Council rates	122
Administration and corporate costs provided (to FACS=DCJ)	117
Interest expense	52
Other operating expenditure	234
(less funding to LAHC from DCJ)	*-90*
Aboriginal Housing Office (AHO)	**123**
Recurrent grants (NP Indigenous Housing)	19
Recurrent grants (other)	6
Personnel services/employee related	15
Depreciation expenditure	21
Repairs and maintenance	24
Council rates	13
Administration and corporate costs provided	9
Other operating expenditures	15
(less funding to AHO from DCJ)	*-60*
Total Expenditure	**2,341**
less LAHC and AHO depreciation	*543*
Total Recurrent (cash) Expenditure	**1,797**

Source: DCJ

4.2.2 Communities Plus (CP)

Initiated by the DCJ, the scheme is a large-scale building program that aims to deliver social, affordable and private housing by partnering with private developers and CHPs. The newly built properties will be located close to employment, education, public transportation and other public amenities. The program is expected to deliver 23,000 new and replacement social and affordable housing dwellings in NSW over the next 10 to 20 years.

The development is also supported by, but not limited to, concessional use of land, exemptions from council rates, tax concessions and eligibility for recurrent funding in the form of NRAS.

4.2.3 Social and Affordable Housing Fund (SAHF)

The SAHF is an initiative that provides funding to private or non-profit social and affordable housing providers through a payment stream from investment returns. Utilising investment returns on a $1.1 billion endowment fund, the program seeks to provide a stable income stream for up to 25 years to cover the gap between the cost of providing and managing a portfolio of social and affordable housing, together with contracted tenant support services. The $1 billion fund is invested in the capital markets by the NSW Treasury Corporation.

The SAHF is a key component of the NSW Future Directions strategy alongside Communities Plus, Community Housing Innovation Fund (CHIF) and Social Housing Management Transfer (SHMT). The scheme aims to deliver 3,400 additional social and affordable homes in NSW by 2023 – that is, some 500 per year over this period. With this outcome the capacity of the fund will be fully exhausted.

The DCJ is responsible for the commissioning and assurance that contractual obligations are met. Two procurement processes have been conducted and a total of nine contracts have been awarded to successful bids.

In the first stage (SAHF1) in March 2017, five CHPs were approved to deliver 2,200 affordable houses in both metro and regional NSW. These providers are:

- BaptistCare NSW & ACT
- UnitingCare
- SGCH Sustainability Ltd
- St Vincent de Paul Housing
- Compass Housing Services Co Ltd

In the second stage (SAHF2) in January 2019, four CHPs were approved to deliver 1,200 dwellings.

- Anglicare
- Housing Plus
- SGCH Portfolio Ltd
- Uniting NSW & ACT

4.2.4 Community Housing Innovation Fund (CHIF)

The CHIF allocates $50 million in grants to CHPs over the next three years. The grants will go towards portions of selected affordable housing projects by CHPs and their development partners, with the rest funded by developers' own equity or debt. The fund aims to support the growth of small to medium sized CHP portfolios.

4.2.5 Social Housing Management Transfer (SHMT)

The SHMT scheme transfers the management of public housing (with sitting tenants) to non-profit community managers (via a 20-year lease) while the title of the properties remains with LAHC (consequently limiting the scope for a recipient CHP to leverage additional investment). The transfer of around 14,000 properties was completed in 2019. With these new properties under management, CHPs can provide housing to a range of eligible tenants. Renting with CHPs also makes tenants eligible for Commonwealth Rent Assist (CRA). This is one of the aims of SHMT, which increases the flow of revenue into the social housing system, thereby reducing the subsidy gap.

4.2.6 Community Housing Leasing Program (CHLP)

The CHLP allows CHPs to acquire properties for social rentals through leasehold or capital purchase (from new developments). The program allows CHPs to acquire properties in locations that are too expensive for governments to acquire directly. Since properties are acquired from the private market, the arrangement provides the tenant with the opportunity to transition from social to private rentals down the track. The market solution also allows CHPs to enter and exit locations much more quickly depending on demand. Funding of approximately $83 million has been provided to CHPs in 2019-20 to provide 5,939 CHLP social housing properties. This is in addition to $4.5 million provided for 270 CHLP homelessness housing properties.

4.2.7 Housing for Seniors or People with a Disability (SEPP)

The State Environmental Planning Policy (SEPP 5) was introduced in the early 1980s to enable special purpose housing developments by private providers. It provides housing for older people, people with disabilities and is not targeted at particular income groups. This is a planning policy which, CHPs, and private sector developers can use to develop housing for seniors or people with a disability. The policy enables the development of group homes, boarding houses, secondary dwellings for any developer (public or private).

4.2.8 Affordable Rental Housing (ARHSEPP)

The Affordable Rental Housing (ARHSEPP) aims to increase the supply and diversity of affordable rental and social housing in NSW. The program covers various housing types including in-fill affordable housing, granny flats, boarding houses, group homes, social housing and supportive accommodation.

4.2.9 SEPP 70 Affordable Housing Revised Schemes

State Environmental Planning Policy No 70 – Affordable Housing Revised Schemes (SEPP 70) identifies the local government areas (LGAs) where councils may place conditions on developments which require inclusionary zoning provisions for affordable housing.

4.2.10 Indirect measures – stamp duties

Stamp duty (also known as transfer duty in NSW) is paid upon the acquisition of property. Stamp duties are one of the most inefficient forms of taxation as they distort the decision-making process in purchasing a property. Ideally, buyers should be able to choose the type of housing best suited to their current and future needs in terms of family size, stage of life and wealth, with tax having no impact on the decision. Stamp duties apply a significant one-off barrier to the decision and so disincentivise owners moving (to find a property better suited to current needs). Also, many older Australians who would like to downsize are effectively locked into their existing homes, while many younger families cannot access or are priced out of the stock of larger houses. However, there are exemptions for lower income households.

4.3 Local level

In this subsection, we describe data from the Australian Bureau of Statistics (ABS) that captures local government expenditure on housing and other amenities. Additionally, at the local government level, the policy of Inclusionary Zoning is discussed as a way for private developers to fund the provision of affordable housing alongside their planned new developments.

4.3.1 Local level - expenditures at local government level

The expenditure on combined housing and community related amenities by the NSW local government councils is estimated to be $550 million in 2018. The custom data provided by the ABS did not detail (in a stand-alone manner) housing expenditure at the local government level.

Table 15 – Local government level expenditures on housing and other amenities

$ million	2010	2011	2012	2013	2014	2015	2016	2017	2018
NSW Local govt	683	647	609	470	529	512	509	554	550
Vic Local govt	105	114	86	102	117	125	99	95	97
Qld Local govt	103	121	132	122	141	141	139	141	161
SA Local govt	64	73	75	99	105	106	115	120	131
WA Local govt	200	291	295	317	356	362	385	399	376
Tas Local govt	18	22	25	25	27	23	23	23	22
NT Local govt	77	73	85	76	70	70	67	62	62

Source: ABS Custom Data

Note: The series contains expenditures not related to the provision of housing.

Expenditure data for NSW and WA appears to be several times that of their counterparts in Victoria and Queensland. Experts expressed surprise upon examining the data and unfortunately could not verify if the data is a faithful representation of actual expenditure.[59] The levels of spending across state and territory governments are shown in Table 15. Expenditures have declined for NSW since 2010 while Queensland, South Australia and WA have seen moderate increases.

[59] The experts did comment on two aspects of local government involvement in housing and amenities: 1. NSW local government has higher levels of community amenity spending than other states, and 2. Most local councils' affordable housing portfolio is targeted to people on moderate income levels. There are very little, if any social housing. Additionally, feedback from authorities from NSW Planning, Industry and Environment indicated that LGA spending on community amenities in NSW could also include contributions from housing developers. Data on expenditure most likely to be held by local councils.

5. Are existing approaches enough?

In this section, we examine whether current government policies are conducive to market-oriented solutions to tackle the housing gap.

Clearly, there's a shortfall of necessary equity investment by governments and the private sector to deliver new housing in sizeable volumes to alleviate the housing shortages. Previous studies by Anthony & Lu (2017) and Troy *et al.* (2019) show that there is capacity within the Federal budget to allocate more funding to meet the national shortfall in social and affordable housing.[60] The resources are there, and what government needs to is acknowledge the urgency of the housing problem and take steps to prioritise those in need of secure housing.

In order to devise solutions, we first need to assess the following:

- What is the size of the problem and ask is the problem getting bigger?
- Whether existing macro and micro policies are widening the housing gap?
- How well targeted are policies?
- Are there inefficiencies and duplications facing providers?
- What are the structural barriers that are deterring greater equity investment in this sector?

Addressing these underlying policy issues is what is required to improve the efficiency of the sector and the return on equity.

We attempt to answer each of our questions in turn below. Before we do, we have collated our key findings to provide a summary of major challenges in trying to close the housing gap in NSW. In below section, Figure 16 outlines the current major funding provision in NSW, the measured outcome in the form of existing housing stock and estimates of shortfalls and unmet demand. These figures demonstrate that more needs to be done to address some of the structural issues in the current policy framework to pave the way for better equity funding solutions. Therefore, it is unsurprising that the Productivity Commission's inquiry into Human Services reform, labelled the current state of social housing as 'broken'.[61]

> *"Australia's social housing system is broken."*
>
> Productivity Commission – Reforms to Human Services Inquiry Report 2018

[60] The study undertaken by Dr. Troy showed building more than 1 million social and affordable housing would cost $8.6 billion a year. In comparison, he estimated negative gearing and capital gains tax discount would cost the budget $11.8 billion a year.

[61] Productivity Commission 2018, *Reforms to Human Services - Inquiry report 2018*, Website accessed 26/11/2019: https://www.pc.gov.au/inquiries/completed/human-services/reforms/report.

The report highlighted the short comings of the current social housing system. These include the lack of choice over the location of public housing, lengthy waiting times, and the type and amount of government financial assistance available to households is inequitable.

Figure 13 – Current measures, outcome, estimated shortfalls and present demand on social and affordable housing in NSW

Housing types	Total commitments	Housing outcome	Estimated shortfalls	Present demand
Social	DCJ, LAHC & AHO $1.8 billion	151,814 units	137,100 units	Homeless 37,715 Social housing waiting list 51,014*
Affordable	CRA $1.4 billion	~2,000 units	~79,400 units	
	NRAS $56.2 million	6,545 units		

Source: NSW Department of Communities and Justice, Productivity Commission, City Futures Research Centre, Homelessness NSW.
Note: Social housing waiting list total number of applicants also includes 4,484 people classified under 'greatest needs'. NRAS funding shown was provided by NSW government.

5.1 Is the problem getting bigger?

The worsening in housing affordability has not been helped by a decade of rapid population growth and the rebound in property prices in the second half of 2019. As housing cost picks up, more and more households experience rental stress. New supply of affordable housing is needed to alleviate price pressures. Unless new equity funding streams become available from government or the private sector and attempts are made to address supply-side structural problems plaguing the current system, it is expected that the housing short fall will continue to grow.

Studies have shown that the size of the current social and affordable housing shortfall is likely to expand moving forward. The current estimate of social housing supply shortfall stands at 137,100 units for the state of NSW, while the affordable housing shortfall stands at 79,400 units, see Table 16.[62] It is expected that a further 76,100 units and 24,100 units of social and affordable housing, respectively, will be needed by 2036, with annual growth in the provision of social and affordable housing to be in the double-digits to cope with the growing demand.

[62] Troy, L., van den Nouwelant, R. & Randolph, B. 2019. 'Estimating need and costs of a social and affordable housing delivery', City Futures Research Centre, UNSW Built Environment, UNSW Sydney.

Table 16 – Additional social and affordable housing needs

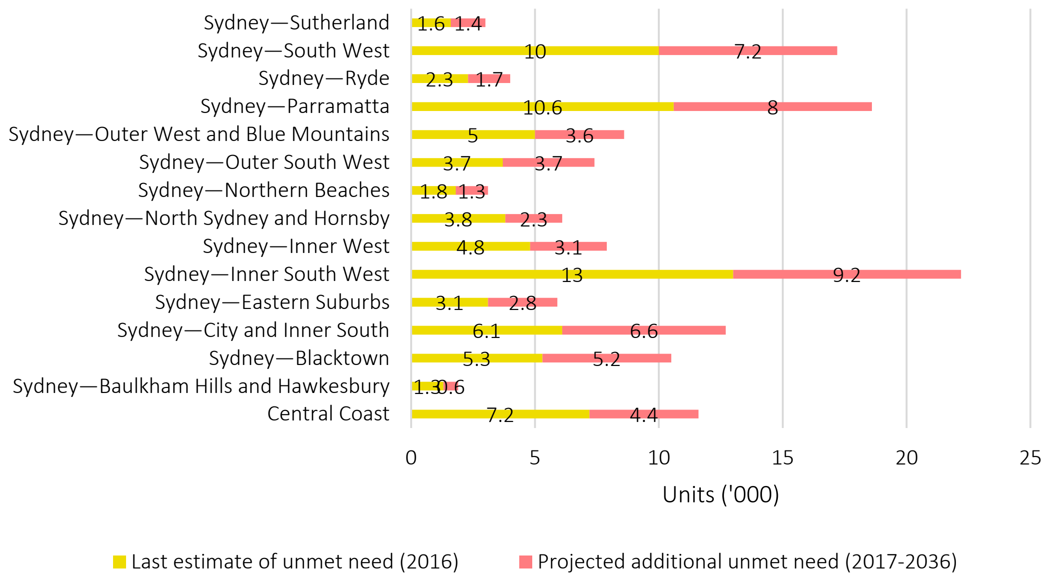
	Current shortfall		Projected additional shortfall by 2036		Total shortfall in 2036		Annual growth needed	
	Social	*Afford.*	*Social*	*Afford.*	*Social*	*Afford*	*Social*	*Afford*
Greater Sydney	80,800	55,300	60,400	20,500	141,200	75,800	22.4%	12.0%
Rest of NSW	56,300	24,100	15,700	3,600	72,000	27,700	46.0%	17.7%

Source: Troy et al. (2019)

Note: AHURI in the report "Social housing as infrastructure: an investment pathway" also estimated that for NSW, the total additional social need between 2016-2036 is 212,700 (140,600 for Greater Sydney and 72,100 for rest of NSW).

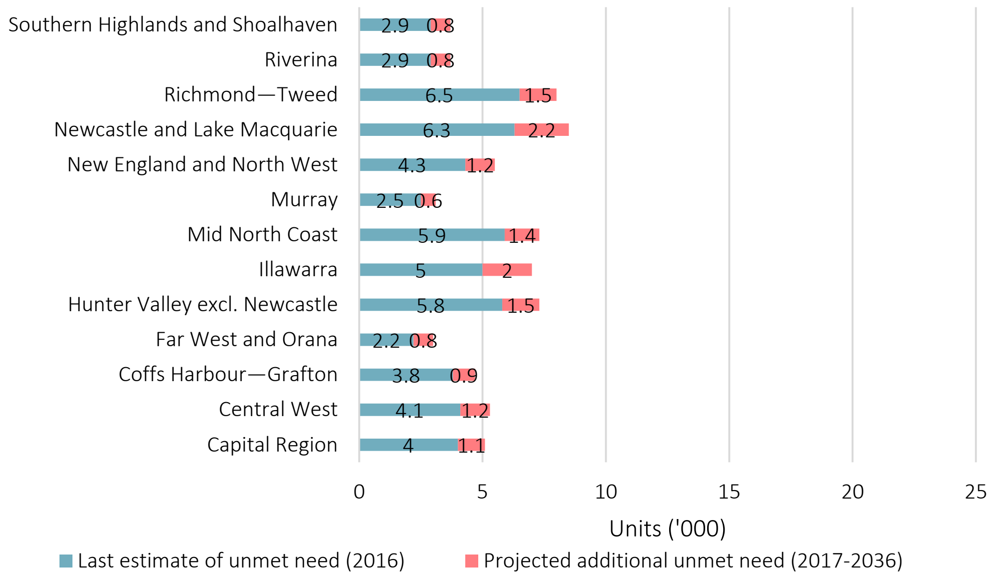
The extent of the unmet need for social housing shortfall going forward varies between regional NSW and (within) metropolitan Sydney. As shown in Figure 14, the level of projected additional un-met social housing need in Sydney between 2017 and 2036 is much more in the south west, Parramatta and inner south west suburbs – totalling 24,400 units. The level of projected unmet needs is much less for regional NSW, see Figure 15.

Figure 14 – Sydney area existing and projected unmet social housing need between 2017-2036 (AHURI)



Source: Lawson et al. (2018)

Figure 15 – NSW regional area existing and projected unmet social housing need between 2017-2036 (AHURI)



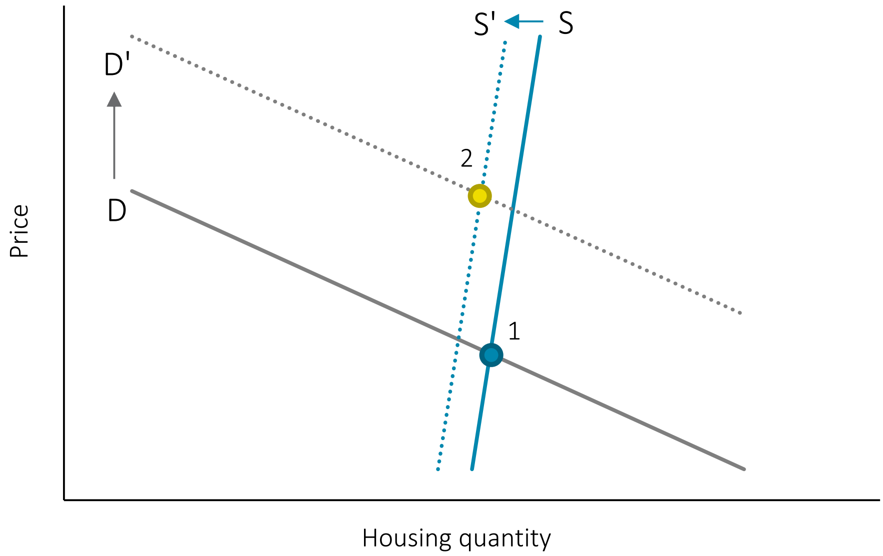
Source: Lawson et al. (2018)

5.2 Is policy inadvertently widening the housing gap?

From the supply and demand perspective, the current mix of Commonwealth and state policies are likely to be insufficient (with some even being counterproductive) to close the housing gap. Current funding levels are evidently enough, but poorly targeted. There are measures that boost housing demand rather than supply which detract from greater equity participation by the private sector.

The economics of the widening housing gap is discussed below. Housing supply is usually inelastic – as Figure 16 illustrates. Prices can rise quickly (from point 1 to 2) as the demand curve shifts up (encouraged by tax incentives, population growth, lower interest rate etc.), while supply is hampered by lack of new funding commitments and deterioration of existing stock. The inelastic nature of supply means it responds to price increases much more slowly.

Figure 16 – Supply and demand measures putting upward pressure on house prices



Source: ISA Analysis

Note: Illustrating effects of rising demand (encouraged by policy measures) with supply curve shifting left (due to public funding plateauing and deterioration of existing stock) resulting in significant price increases.

We explore the following list of measures and how they're impacting the supply and demand balance. We shall start with demand:

5.2.1 Demand

Policies listed below may be indirectly contributing to housing demand and worsening affordability in large cities such as Sydney and regional centres.

- Fiscal - tax policies are priming demand and worsening affordability

The rising demand for public housing and homelessness services is a direct result of worsening affordability in the housing market. Existing tax concessions such as the capital gains tax (CGT) discount and negative gearing are encouraging investor demand in the housing space while doing nothing to directly boost new construction to improve housing affordability. It is estimated these measures cost the Commonwealth budget up to $15 billion annually.[63]

- Budgetary policies that aim to raise home ownership may be contributing to demand
  - The state of NSW provides first home buyers with stamp duty relief and up to $10,000 in grants to reduce their financial burden.[64]

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[63] Dawson, E. & Smith, W. 2018, 'The Cost of Privilege – A Research Paper by Per Capita for Anglicare Australia', Per Capita. Website accessed 23-01/2019: https://percapita.org.au/wp-content/uploads/2018/05/Cost-of-Privilege-Report-7.pdf

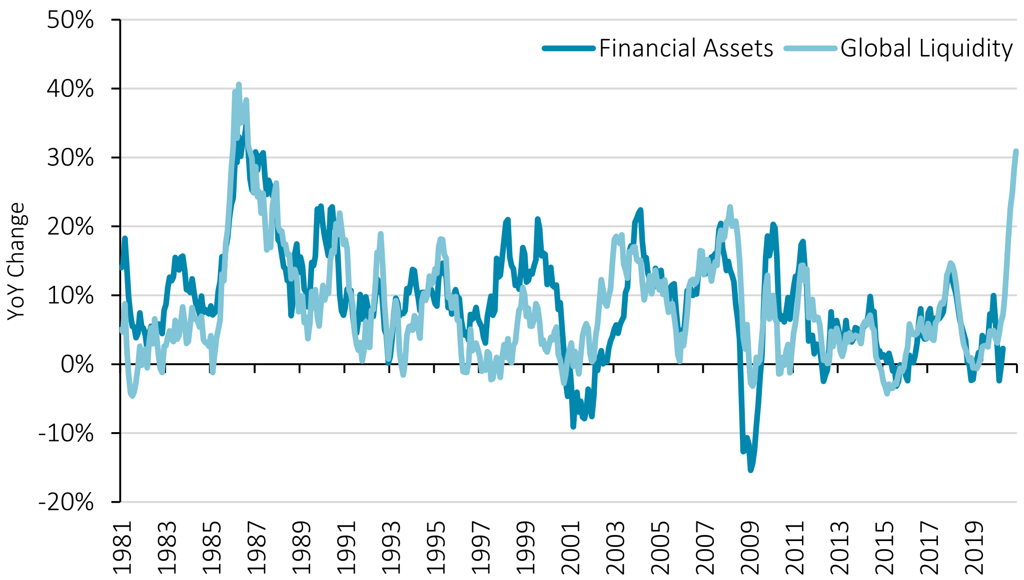
[64] The incentives for first home buyers include abolishing stamp duty on all homes up to $650,000; give stamp duty relief for homes up to $800,000; provide a $10,000 grant for builders of new homes up to $750,000 and purchasers of new homes up to $600,000 and abolish insurance duty on lenders' mortgage insurance.

- The new First Home Loan Deposit Scheme (started on 1 January 2020) was introduced by the Commonwealth and allows first home buyers to purchase a home with a deposit as low as just 5 per cent. Recipients have their home loan guaranteed by NHIFC (15 per cent value of the property).
- The Commonwealth introduced in the 2017-18 Budget the First-Home Super Saver Scheme (FHSSS). It allows buyers to pool voluntary contributions that would go towards their deposit on their first home.[65]
- The Senior Downsizing Scheme (SDS) also introduced in the 2017-18 Budget, encourages seniors to transition from their existing family home to a smaller home, and contribute the sales proceeds (up to $300,000) to their super accounts in the form of non-concessional contributions.

Monetary and prudential policy

Monetary and prudential policy as practiced by major central banks from the mid-1990s have tended to drive global liquidity by relying more heavily on the pure wealth and collateral transmission mechanisms leading to global asset price growth (Figure 17). This has tended to disincentivise business lending (a risky proposition) relative to residential property lending (preferred collateral). The wall of global liquidity expansion has certainly impacted Australian domestic property markets especially in Sydney and Melbourne, with the advent of China's manufacturing boom and the expansion in Australia's temporary migrant visa system from the mid-2000s onwards.

Figure 17 – Global liquidity and financial asset prices



Source: CrossBorder Capital

Perhaps the RBA and the Australian Prudential Regulation Authority (APRA) did not fully consider the inflationary impact of current policy mix in terms of the relationship between

[65] Under the scheme, an individual would be allowed to make voluntary contributions of up to $15,000 per year and up to $30,000 in total. These amounts, along with earnings can be withdrawn from their super fund after 1 July 2018.

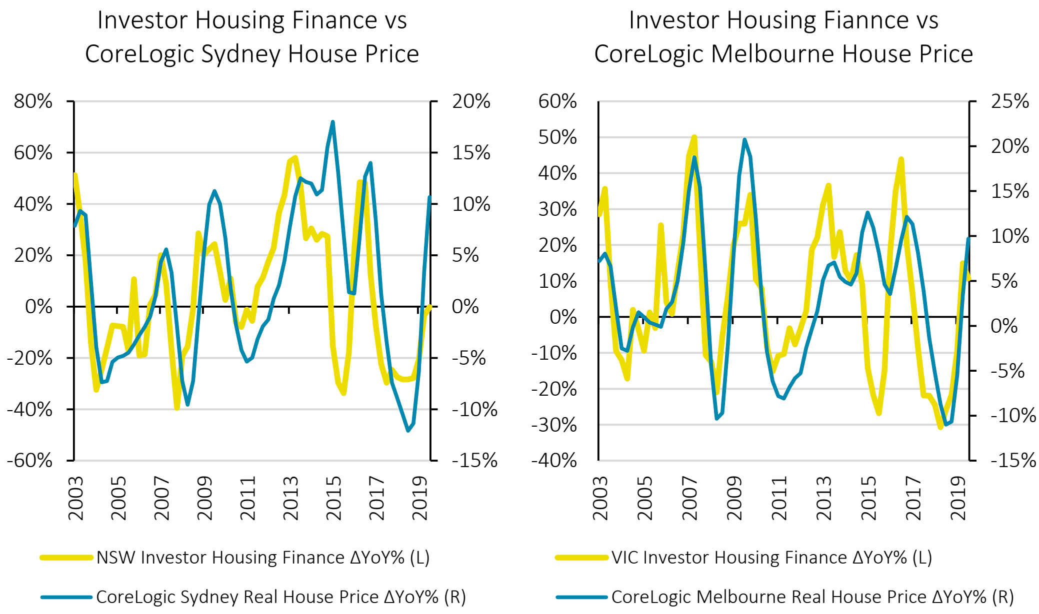
credit provision and property values (Figure 18). We map changes in Sydney and Melbourne property prices in this chart to total new credit provided by financial institutions for housing in NSW and Victoria. The focus is on housing credit (rather than policy interest rates) and reflects the reality that whilst the RBA initiates lending via policy levers, banks relied on lending against collateral and offshore borrowing.

The operation of monetary policy in Australia and overseas in the post financial deregulation era from the mid-1980s onwards was very different to the Post World War II expansion period.

- During the earlier period across the OECD, central banks were subordinated to ministries of finance that focused more on national development, whilst leaving central banks with a wide set of stabilisation goals (Ryan-Collins 2019).
- During the later period across the OECD, the combination of independent central banks and inflation targeting, and perhaps a relatively benign macro policy environment before the GFC, lead to over confidence in the monetary policy toolbox in terms of its ability to directly achieve its targets without adverse side-effects.

The collapse of the mining investment boom by late 2012, saw the RBA actively fostering the conditions for a residential real estate boom via the pure wealth and collateral transmission mechanisms to drive to spur consumer spending.[66] Some may say this was far-sighted, pre-empting what Ross Garnaut described as the coming Dog Days (Garnaut 2013). But as a policy mix it constituted what Andy Haldane (2015) described as short-termism because it ‘kicked the policy can down the road’. Our national history also suggests that property booms precede an eventual bust. This lesson was certainly reinforced in United States during the GFC.

Figure 18 – Australian historical credit and land value



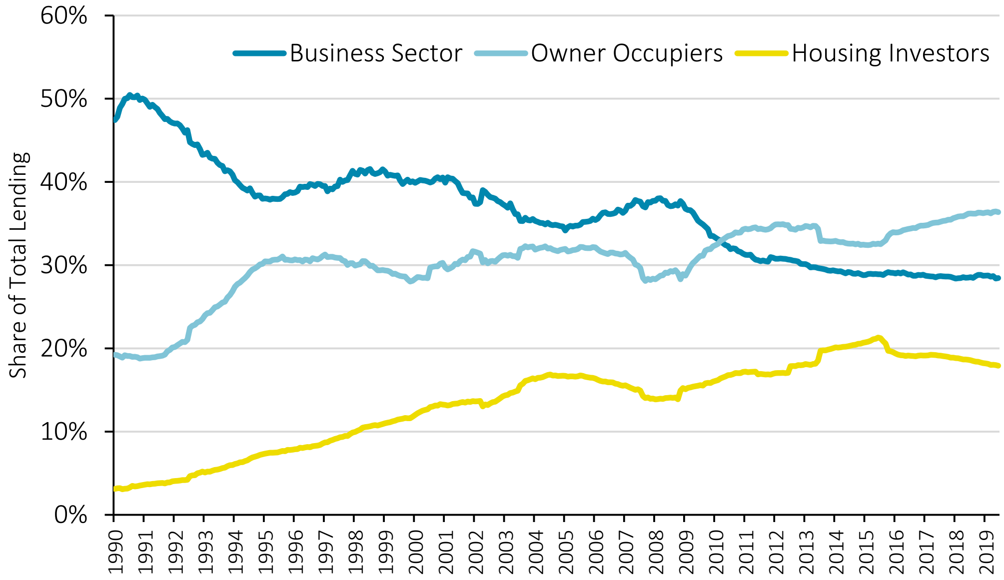
Source: ABS5601.0, DataStream, CoreLogic

Note: Investor housing finance excludes refinancing, for new loan commitments only.

[66] Lowe, P. 2015, ‘National Wealth, Land Values and Monetary Policy’, speech, Address to the 54th Shann Memorial Lecture, Perth, 12 August 2015. Website accessed: 27/07/2020, URL: https://www.rba.gov.au/speeches/2015/sp-dg-2015-08-12.html

At the same time, it can be argued the RBA and APRA have not sufficiently focused on the allocation to credit to SMEs relative to investor loans for mum and dad investors (Figure 19). It seems there is a genuine market failure occurring in Australia in the provision of capital (perhaps both debt and equity) to small and medium-sized enterprises. This is supported by the RBA firm level research, which has quantified this funding gap at around 500 basis points, controlling for all other factors including risk (RBA 2018).

Figure 19 – Business lending as share of total lending on the decline



Source: RBA Statistics – D5 Bank Lending Classified by Sectors

5.2.2 Supply

The supply of social and affordable housing has been constrained mainly by the lack of public new equity funding committed to increasing the housing stock.

- NHHA – no real increase in funding

The new NHHA agreement broadens the policy breadth that aims to improve housing outcomes across the housing continuum. However, whilst it maintains the $1.3 billion in funding, there has been no increase in real terms. Considering measurable increases in rental stress, homelessness and the ageing population, Milligan 2019 argued that: [67]

- The new agreement falls short of a comprehensive national strategy that should include policy alignment on taxation, immigration and rent assistance.
- Performance targets for the old NAHA were replaced by new measures on progress, which raises concern about accountability.

[67] Milligan, V. 2018, 'The new national housing agreement won't achieve its goals without enough funding', *The Conversation*, 17 July 2018, Website accessed 22/11/2019: https://theconversation.com/the-new-national-housing-agreement-wont-achieve-its-goals-without-enough-funding-99936

- A funding deficit remains with this new agreement as the Commonwealth has failed to extend or replace the NRAS and the national partnership to improve housing supply and conditions in remote communities.

NRAS – inefficient, costly and yields affordability of limited duration

Whilst it's estimated that NRAS has delivered more than 5,800 affordable rentals in NSW and tens-of-thousands more across the country, concerns about complex administration, poor targeting and administrative delays resulted in the discontinuation of the scheme in May 2014.[68] As NRAS subsidies did not vary by location or size of dwelling, in some cases, investors received more dollar incentives from the government than was required for a 20 per cent discount from the market rent. This resulted in significant windfalls for some lucky private investors at the expense of taxpayers.[69]

NHFIC – debt financing alone won't address affordability issues

While NHFIC is a source of low-cost, efficient financing for affordable housing development, a funding gap is still present and requires alternative strategies to supplement the cost of affordable housing development. A study by Lawson *et al.* (2019) has found that reliance on commercial finance not only would increase the operating cost for CHPs, but also requires a higher level of Commonwealth subsidy during the operating phase. Long-term financing provided by the NHFIC brought down financing cost, but 'financing alone is not sufficient to address deep affordability needs'.[70] Some form of public equity investment has been argued as the most cost effective form of financial support over the long term, although the near-term impacts on government budgets make this politically even more challenging than re-structuring existing subsidies via recurrent payments (e.g. as under SAHF).

Public housing in decline and in poor condition due to lower public investment

Inadequate public investment has virtually frozen the social housing stock since the 1990s. There was a brief uplift under the Commonwealth's 2009-2011 Social Housing Initiative. However, this made little impact on the scale of unmet demand.

There has been a major ideological shift in social and settlement policy in Australia since 1990. Previously, from 1945, government programs built 8,000-14,000 dwellings a year for half a century before public housing slipped off the agenda.[71]

A study conducted by Ong *et al.* (2019) shows when it comes to unmet demand for public housing, Sydney tops the list with over 150,000 households (118,919 for rest of the NSW).

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[68] Rowley, S., James, A., Gilbert, C., Gurran, N., Ong, R., Phibbs, P., Rosen, D. and Whitehead, C. 2016, 'Subsidised affordable rental housing: lessons from Australia and overseas', AHURI Final Report No. 267, AHURI, Melbourne, Website accessed 22/11/2019: https://www.ahuri.edu.au/research/final-reports/267.

[69] Coates, B. & J. Horder-Geraghty 2019, 'Learning from past mistakes: lessons from the National Rental Affordability Scheme', Grattan Blog, September 2019. Website accessed 22/11/2019: https://blog.grattan.edu.au/2019/09/learning-from-past-mistakes-lessons-from-the-national-rental-affordability-scheme/.

[70] Lawson, J., Denham, T., Dodson, D., Flanagan, K., Jacobs, K., Martin, C., Van den Nouwelant, R., Pawson, H. and Troy, L. 2019, 'Social housing as infrastructure: rationale, prioritisation and investment pathway', AHURI Final Report No. 315, AHURI, Melbourne. Website accessed 22/11/2019: https://www.ahuri.edu.au/research/final-reports/315.

[71] Lawson, J., Pawson, H., Troy, L. & Van den Nouwelant, R. 2018, 'Australia needs to triple its social housing by 2036. This is the best way to do it.' *The Conversation*, 15 Nov 2018, Website accessed 22/11/2019: https://theconversation.com/australia-needs-to-triple-its-social-housing-by-2036-this-is-the-best-way-to-do-it-105960.

These are households that are renting privately but eligible for public housing. NSW and Victoria account for 55 per cent (518,000) of all households eligible for public housing. Table 17 shows the estimated unmet demand for Sydney, rest of NSW and Australia.[72]

Table 17 – Population estimates of households residing in private rental housing yet eligible for public housing, all ages, 2016

State breakdown	Number of households eligible for public housing	% of all private rental households	% of all households
Sydney	157,008	27%	9%
Rest of NSW	118,919	45%	11%
Australia	941,356	36.8%	10.2%

Source: Ong et al. (2019)

The other major aspect of the housing decline is the poor condition of public housing highlighted by the Productivity Commission (2020), where approximately 24 per cent of NSW public housing tenants in 2018 live in unacceptable conditions.[73]

- **Short-term letting (STL) platforms are taking long-term rentals out of the market**

The availability of STL platforms such as Airbnb provides an additional channel for investors to monetise their properties, thereby excluding them from use as long-term accommodation. This most likely impacts the affordability of rentals in the inner-city (and in high demand locations) while cross-city impact is less likely. According to Crommelin *et al.* (2018), the availability of the alternative monetarisation channel adds another factor that makes the housing market more fluid[74]. As a result, this reduces the market's ability to provide a steady and sufficient supply of affordable long-term housing.

- **Other indirect measures that are hampering housing supply**

Restrictive and inflexible town planning rules are limiting the increase in housing densities in urban 'inner' and 'middle-ring' suburbs.

  - The Department of Planning, Industry and Environment promoted the "Missing Middle" to encourage low rise medium density housing developments, but this was met with pushback from local councils fearing NIMBY backlash from their communities.
  - Both the public and private sectors are holding significant tracts of land that are suitable for affordable housing developments. The problem is compounded by the fragmented pattern of ownership.

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[72] Ong, R., Wood, G., Cigdem-Bayram, M. and Salazar, S. 2019, 'Mortgage stress and precarious home ownership: implications for older Australians', AHURI Final Report No. 319, AHURi, Melbourne. Website accessed 22/11/2019: https://www.ahuri.edu.au/research/final-reports/319.

[73] An acceptable dwelling standard refers to the dwelling having at least four working facilities (for washing people, for washing clothes, for storing/preparing food, and sewerage) and not more than two structural problems.

[74] Fluidity refers to i. the flexibility and frequency that owners can convert properties from long-term letting to short-term letting and vice-versa, ii. the expansion of financialised attitudes towards housing, and iii. taking into consideration hosting options into the investment decision making process.

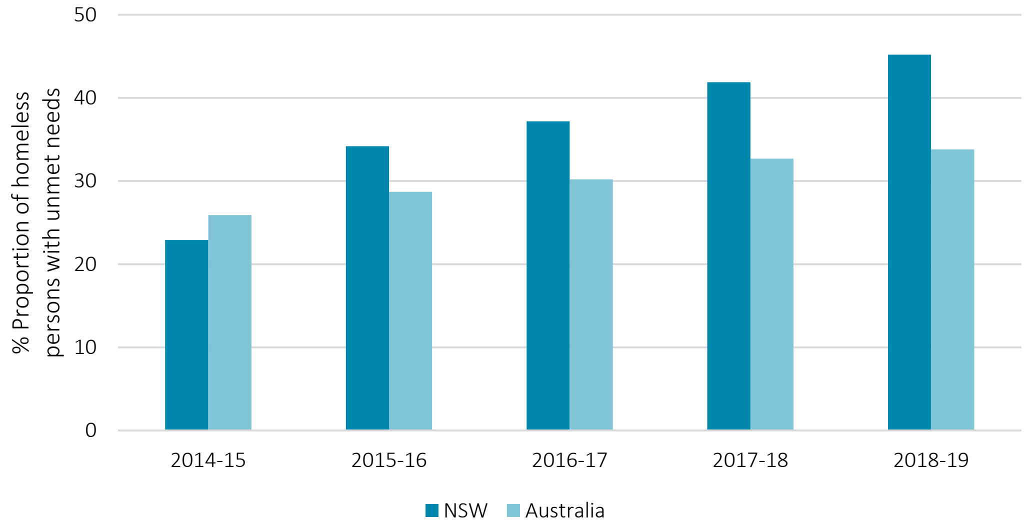
5.3 Are housing policies well targeted?

Whilst resources have been put in place to address the housing gap, the lack of an effective mix of policy measures that expands equity investment into the social and affordable housing sector is constraining the growth of the sector.

Accommodation services unable to cater for all homelessness needs

The latest findings on homelessness from the Productivity Commission shows the proportion of unmet demand for accommodation for the homeless has grown every year in NSW since 2014. As shown in Figure 20, 45.2 per cent of the homeless population in NSW surveyed reported a need for accommodation services in 2018-19, that was unable to be met. The chart shows the growth rate in unmet need for NSW is higher than the national total, highlighting the severity of affordability problems in the State.

Figure 20 – Unmet demand for accommodation services among the homeless in NSW

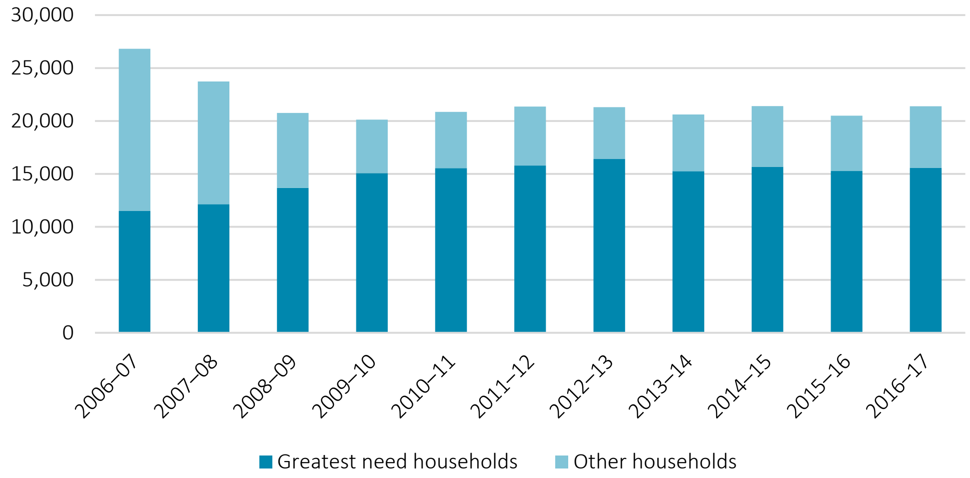


Source: Productivity Commission Report on Government Services 2020
Note: Need for accommodation includes need for 'Short-term or emergency accommodation', 'Medium-term / transitional housing' or 'Long-term housing'.

Allocations to households with greatest needs came at the expense of other households

Data reported by the Australian Institute of Health and Welfare shows for public housing, the number of new allocations (nationally) to households in greatest need has been rising since 2006-07, see Figure 21. Over the same period, the number of new allocations to other households has decreased. In effect, due to supply constraints, allocations towards 'other households' have not experienced any significant increase since 2006 or within the 11-years of data analysed. This means households eligible for public rental but in less severe circumstances than those classified under 'greatest needs' are been forced to wait.

Figure 21 – Number of newly assisted households in public rental housing (national)



Source: Australian Institute of Health and Welfare

5.4 Are inefficiencies and duplications present?

CHPs play an integral role in the development and operation of affordable housing assets. However, recent feedback from CHP stakeholders has revealed concerns over regulatory compliance burdens and instances of duplication in the current framework.[75] Streamlining and reforming current regulatory arrangements is clearly needed to improve efficiency and bring confidence for greater investment into the sector.

CHPs concern centres on the National Regulatory System for Community Housing (NRSCH), which is a national system of registering, monitoring and regulating CHPs. Whilst agreeing to the need for regulation, they question the way it has been implemented:

- Regulatory duplication

The current structure of national and state level community housing regulatory frameworks means some reporting and compliance requirements between NRSCH and other frameworks are duplicated which adds to the burden of their operation. In many instances, CHPs face difficulties in working across multiple jurisdictional frameworks for community housing.

- Inefficiencies in the current reporting arrangements include limited timing, duplicative reporting of documents under different performance outcomes and the resource burden (time spent on administrative work instead of delivering frontline services) of registration and compliance processes.
- Duplication of reporting was also a common concern amongst CHPs, with some arguing that the sector may be over-regulated. Examples include multiple and conflicting definitions, datasets, systems, reporting templates and timing.

[75] This was part of a review into the NRSCH and feedback was provided by CHPs and relevant peak bodies. Department of Communities and Justice (NSW) 2019, *The Review of the National Regulatory System for Community Housing (NRSCH) - Discussion Paper*, NRSCH Review Working Group, Website accessed: 16/01/20: https://www.facs.nsw.gov.au/download?file=672867

- It was also reported that some CHPs have experienced 'duplication between NRSCH and government funding contracts, as well as between different contracts within a single agency, across all levels of government'.

A whole of government approach

Areas of duplication with other regulatory systems and some contracting requirements need to be removed whilst adopting a consistent national framework. This would avoid the need to setup multiple housing entities across the states and territories.[76]

5.5 Other structural barriers to equity participation

Whilst policies that help lower the cost of affordable housing development (e.g. cheaper debt available via NHFIC) are clearly welcomed by CHPs and socially conscious investors alike, impediments remain over greater institutional investments through equity in this sector.

Some of the barriers to greater institutional investments in Australia can be attributed to the nature and nascency of the affordable housing asset class in Australia, while others stem from uncertainty over government commitment to the consolidation of this asset class. Below is a list of potential barriers to large scale institutional investment in affordable housing.

Complexity in planning, construction and tenancy management

Affordable housing construction and development may require complex administration due to the possibility of managing planning, regulation and taxation issues across different jurisdictions, in conjunction with the requirement to possess or access financial expertise in raising funds from multiple sources. Once in its operational phase, affordable housing may require more intensive management due to higher level of maintenance, and reputational risk associated with evictions in the event of a default.[77] As found by AHURI:

> *"Investors are interested in completed, tenanted projects with no development risks."*
>
> Lawson *et al*. 2014
> – Enhancing affordable rental housing investment via an intermediary and guarantee

Policy inconsistency and uncertainty

As the investment horizon (how long you plan to stay invested) for affordable housing is at the long end of residential asset class, it is important that there is consistency and certainty over policy and regulatory settings, to give support to a more predictable investment outlook with more certainty on investment value and cash flow.

Lack of incentives in tax policy

Current taxation laws mean institutional investors are less able to realise a profitable return from residential property, let alone affordable housing. According to AHURI, the following are

[76] The Salvation Army has separate housing entities throughout Australia due to 'three different regulatory systems'. St. Vincent de Paul Society does not operate in Victoria as the state is not a participant in the NRSCH. *Ibid.*

[77] AHURI 2018, *Attracting large institutional investors for affordable housing developments*, Policy Issue Analysis, AHURI. Website accessed 17/12/19: https://www.ahuri.edu.au/policy/policy-analysis/institutional-investment.

some of the existing tax measures that potentially are disincentivising against greater institutional investment:[78]

- Superannuation funds only receive 33.3 per cent discount on capital gains as compared to the 50 per cent discount extended to individual investors.
- Superannuation funds cannot directly borrow to buy property and hence cannot claim mortgage costs.
- Companies, superannuation funds and individual investors allocate capital in many residential properties that are liable for land tax and stamp duty. Again, because of the way that state/territory land tax frameworks are structured, they disadvantage or disincentivise larger scale (e.g. institutional) investors relative to individuals or smallholding landlords.

Other tax settings such as GST treatment of build-to-sell (BtS) versus build-to-rent (BtR) creates an uneven playing field for institutional investment. BtS projects are effectively exempt from paying the GST, but this exemption does not extend to BtR projects, which makes investment in the latter less attractive.[79]

Having suitable tax incentives and removal of unfavourable treatments would make investment in the sector much more appealing to institutional investors.

Lack of scale

Regulators and CHPs need to establish suitable deal size to attract large institutional investors. Typically, individual institutions in Australia expect investments to range between $50 million to $250 million, and at least $500 million in aggregate per annum, to create liquidity and market sustainability.[80] This means the fragmented nature of existing investment opportunities needs to be resolved.

Short performance history

Investor confidence in the sector is hampered by the lack of performance track-record which provides the asset's risk-return profile. Additionally, the performance of the organisation's managing the affordable housing stock needs to be established to minimise counterparty risks.

Illiquidity of assets

Like other property and infrastructure investments, entering and exiting such assets is a long process and is significantly more complex and riskier compared to market tradable assets such as bonds and equities. With affordable rental housing, the additional work involved with termination of tenancy also complicates the transaction process. Careful consideration needs to

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[78] AHURI 2018, *Attracting large institutional investors for affordable housing developments*, Policy Issue Analysis, AHURI. Website accessed 17/12/19: https://www.ahuri.edu.au/policy/policy-analysis/institutional-investment.

[79] Pawson, H, Martin, C., van den Nouwelant, R. & Milligan, V. 2019, 'Build-to-Rent in Australia: Product feasibility and potential affordable housing contribution', LANDCOM. Website accessed 21/02/2020: https://cityfutures.be.unsw.edu.au/documents/551/LCOM_0000_Build_to_Rent_Report_WEB_July_2019.pdf

[80] AHURI 2014, 'How can government encourage institutional investment to increase the supply of affordable housing?', AHURI Research and Policy Bulletin, Issue 175, July 2014, AHURI. Website accessed 17/12/2019: https://www.ahuri.edu.au/__data/assets/pdf_file/0021/2919/AHURI_RAP_Issue_175_How-can-governments-encourage-institutional-investment-to-increase-the-supply-of-affordable-rental-housing.pdf.

take place as investment decisions in affordable housing may not be (easily) reversible if investment priorities change.

- Lower returns

The risk-adjusted rate of return on affordable housing is viewed as too low by institutional investors. With typical returns from residential property ranging 4 to 5 per cent, returns for affordable housing would be even lower without ongoing financial support or guarantee from the government.

6. Attracting investment and driving market efficiency

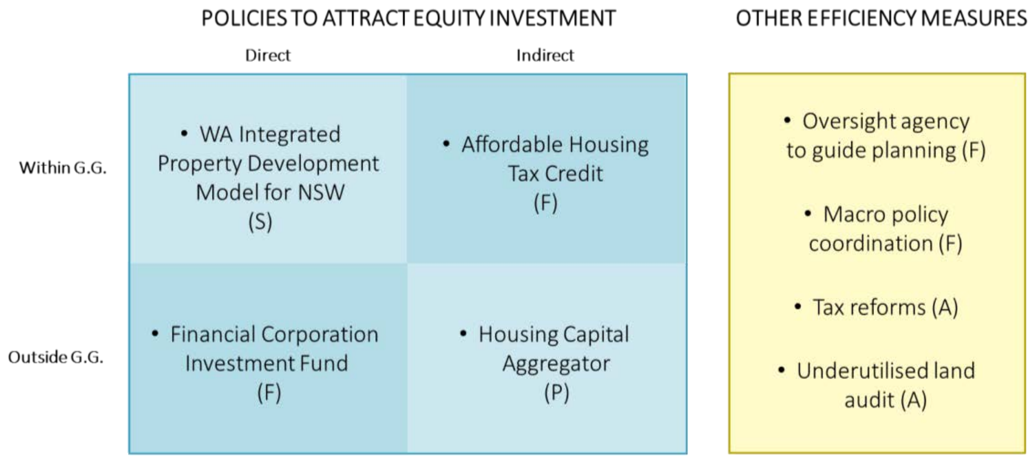
In this section we will explore ways to attract greater equity investment into affordable housing projects. Pulled apart by both policy and market forces, the housing gap is worsening in NSW. Governments need to view the problem as a distributional issue instead of market failure, and policies need to be devised to repair the gap to prevent the social fabric of our society being torn apart. The goal is to direct long-term equity into the sector in a self-sustaining manner.

The lack of equity funding has frequently been cited as the main challenge in bridging the affordable housing gap. This section investigates funding models that encompass direct and indirect government involvement in driving investment, as well as 'on' and 'off' options in terms of impacts of general government cash budgets (Figure 22).

- The direct category options include the WA Integrated Property Development model and Financial Corporation Investment Fund.
- The indirect category includes the Affordable Housing Tax Credit and mainly private sector-based Housing Capital Aggregator.
- The 'on' budget category option includes the WA Integrated Property Development model and Affording Housing Tax Credit.
- The 'off' budget category option includes the Financial Corporation Investment Fund and the mainly private sector-based Housing Capital Aggregator.

We believe these equity investment measures should be considered as part of broader policy reforms to further the future developments in the affordable housing sector.

Figure 22 – Attracting equity investment in affordable housing and supporting economic efficiency in property markets



Source: ISA Analysis

Note: S – state level. F – federal level. A – all levels of government. P – private sector. Horizontal categories - direct and indirect refers to the level of government sector involvement. Vertical categories - within and outside general government (G.G.) P/L or balance sheet.

In addition to policies that attract greater equity investment into affordable housing projects, we suggest structural policies to assist efficient property markets across the nation. These include:

- a national body which identifies shortfalls and bottlenecks in supply and shortcomings in planning systems;
- a macro policy mix (both monetary / prudential and fiscal policy) that better supports / balances housing market imbalances and helps to normalise unimproved land over time;
- tax reforms including replacing stamp duties with a broad land tax;
- an audit of the underutilised land sites across Australian governments; and

We believe these measures will assist to smooth the boom-bust property cycle, complementing policies which drive greater equity investment into affordable housing.

It is also important to highlight that whilst some of these models utilise to the greatest extent institutional and not-for-profit capital, there is still the need for incentives from all levels of government to make the construction and operation of affordable housing financially feasible.

6.1 Policies to attract equity investment

In this subsection, we present four policy proposals and four efficiency measures that would aid equity investment in affordable housing. The policy proposals differ according to their level of government involvement and whether they are 'on' or 'off' general government cash budgets. There are no 'silver bullets' here, nor are policies intended to be stand-alone or exist in a vacuum. What we are saying is that better outcomes can be achieved through time by backing a better mix of policies.

6.1.1 Direct involvement by government

These funding models rely on government taking a leadership role in the planning and management of affordable housing development projects.

The Western Australian Integrated Development model (state level)[81]

The WA Integrated Development model is an integrated, large-scale and comprehensive approach towards the planning, provision and construction of social and affordable housing which factors in broader residential market property signals.[82]

The WA state government, through the Housing Authority, partners with community and private sector organisations to plan and deliver housing options across the housing continuum. The State Affordable Housing Strategy 2010-2020 established wide-ranging goals that included the delivery of social housing, discounts to market rentals, shared equity and affordable home purchase options, and Keystart loans (to encourage home ownership). The measures on offer are intended to ensure the provision of social and affordable housing and aimed at keeping

[81] The model is based on the core functions of the WA Housing Authority prior to December 2019. As the Housing Authority has been part of the Department of Communities for 3-years, there are signs that changes could be coming soon.

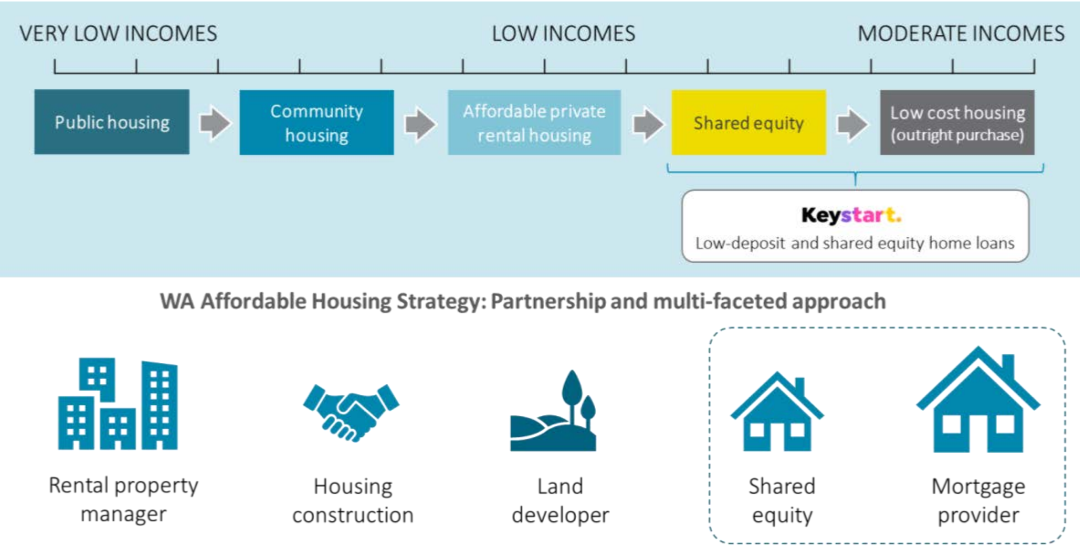
[82] Feasibility of this model in NSW would be dependent on maximising the use of existing government owned land.

prices down for those wanting to purchase housing by maintaining an adequate supply of affordable housing stock.

The goal of maintaining an adequate supply of affordable housing stock is promoted by four key work programs – social rental property management, housing construction, land development and mortgage provision via government lender Keystart.

- To provide social rental housing, the Housing Authority constructs, purchases and manages tenancies; and works with not-for-profit sectors to provide rental housing for people on very low to low incomes;
- The Housing Authority releases government land to be developed by its private partners.[83] As a condition of its release, a certain percentage of housing constructed needs to be affordable for low to moderate income households and these dwellings (delivered by the Housing Authority) range from social housing to affordable sales.
- The supply of affordable vacant residential land puts downward pressure on land prices, particularly at the lower price end of the market. Revenues from land sales are used to subsidise the operating costs of social housing and other housing programs; and

Figure 23 – The WA Integrated Development model



Source: Housing Authority – Department of Communities (WA)

- The approach seeks to influence the supply, range and diversity of affordable housing as well as the demand-supply balance in the broader WA residential property market. Facilitating affordable home ownership reduces additional demand on the rental sector, including social rentals.

[83] The WA Housing Authority has the ability to undertake development of any density within its commercial means. It has several Committees that form the decision-making governance based on delegation and size of investment/project.

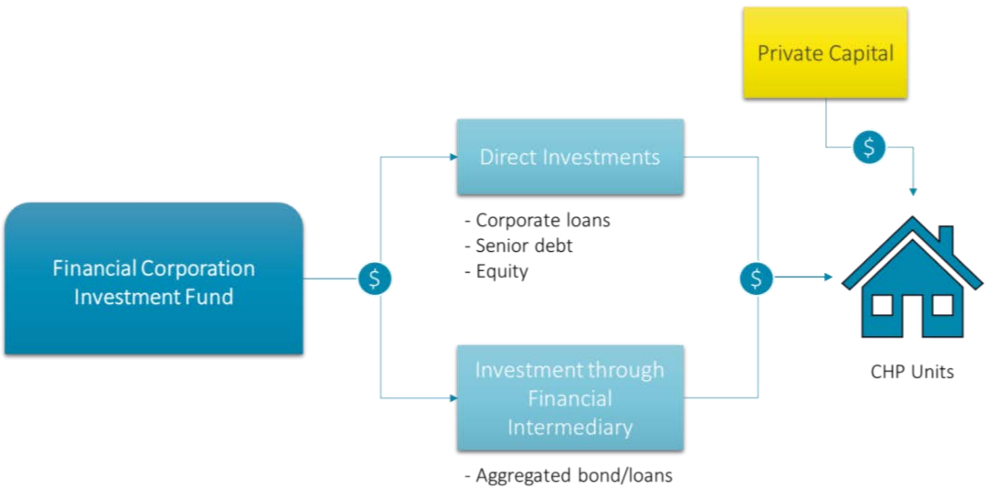
Financial Corporation Investment Fund (FCIF) (Federal level)

The FCIF is intended to be an independent entity formed by the Australian government to facilitate increased financial flows into the social and affordable housing sector. The fund would be capitalised by an initial equity injection from the Australian government (general government sector). Therefore, the operations of the fund would exist outside the funding envelope of the general government cash balance.[84]

The FCIF would invest into affordable housing proposals guided by a rate-of-return (RoR) benchmark. The RoR benchmark would be set at an appropriate discount to market, in consultation with a panel of independent actuaries and commercial property experts. A vigorous investment selection and review framework would need to be established to guide project selection and to establish appropriate performance benchmarks.

The originators (property developers) receiving the investment dollars would include a range of registered not-for-profit (mainly CHPs) and (where appropriate) registered for-profit housing providers. A transparent and rigorous tendering process would be required to ensure developers are selected based on their ability to deliver the best solution for a given funding amount (no pork-barrelling). Funding flows into the CHPs would either come directly from the FCIF in the form of equity or debt (via NHFIC), or through intermediaries such as banks, capital aggregators and other investment funds.

Figure 24 – The Financial Corporation Investment Fund model



Source: ISA Analysis

It is hoped that investments under such a model would attract private sector co-investments into the affordable housing space that otherwise would not occur due to perceived low risk-adjusted returns. The NHFIC could potentially be merged with the FCIF to engage in coordinated investment activities.

[84] The FCIF is intended to take equity investment in affordable housing off general government balance sheet. As the initial injection of funds is equity investment, it will not impact the underlying cash balance. However, for example, if the initial injection is financed via debt (which necessitates interest expense), this will impact the bottom line. But this approach benefits from the current very low interest rate environment.

6.1.2 Indirect government involvement

These funding models rely on the private sector developers and financiers to construct new affordable housing subsidised in part by concessions provided by government.

The Affordable Housing Tax Credit (Federal level)

The Affordable Housing Tax Credit is an offshoot of the cash flow tax first proposed by Garnaut *et al*. (2018) to mitigate the problem of multinationals offshoring profits to overseas tax havens. One of the key features of the cash flow tax is the ability to allow companies making a loss to trade ATO certified tax credits with companies making a profit, which calls for an open market for trading such credits. Extending the concept of tradable tax credits to equity funding for affordable housing would see the Federal government distributing tax credits to accredited developers of affordable housing. These could then be passed onto institutional investors or an 'intermediary aggregation fund' in exchange for equity or debt financing of affordable housing developments.

An outline of the proposed Affordable Housing Tax Credit is shown in Figure 25:

- Accredited/government regulated community housing developers would be provided with contestably allocated tax credits upon successfully tendering for an affordable housing construction project.
- These tradable tax credits would then be passed onto an institutional investor or an 'intermediary aggregation fund' in exchange for equity or debt financing.
  - An aggregation fund is a collective vehicle specifically designed for the purpose of funding multiple affordable housing projects by utilising specialist expertise in this activity to acquire a manager's premium.

Extending equity funding is the critical missing link in the supply chain for development of affordable housing. CHPs relying on debt alone (via bank/NHFIC term lending) will never achieve the scale necessary to deal with the supply gap that has emerged across Australia. For example, we understand that the cash flow generated by rental dwellings can only support debt equal to approximately one third of build costs). But a tax credit can help to build scale and professionalism across the affordable housing sector.

A. Direct exchange of tax credits and equity financing

Through the purchase of tax credits, institutional investors would become active participants in the delivery of affordable housing development project. They would be mandated by Federal or state authorities to ensure projects are delivered as promised in terms of affordability, quality and quantity. Their risk would be mitigated by the regulation of the non-profit community housing industry.

The key appeal to institutional investors would be the use of tax credits to reduce their tax liabilities, while not having to maintain an ongoing equity stake in the affordable housing asset class – the timing of investment **write-off** would vary (subject to the deal) from the completion of the construction phase to the end of the investment term (e.g. 10 to 15 years).[85]

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[85] Timing of the write-off would depend on actual arrangements. The option is open to investors wishing to remain invested for an extended period of time (and receiving a recurring stream of tax credits) prior to exiting or immediate write-off after project completion.

B. Indirect exchange of tax credits via 'intermediary aggregation funds'

Rather than dealing directly with housing developers, an opportunity exists for an 'intermediary aggregation fund'[86] that could offer equity and debt financing options to developers in exchange for tax credits, which would be passed onto institutional investors.

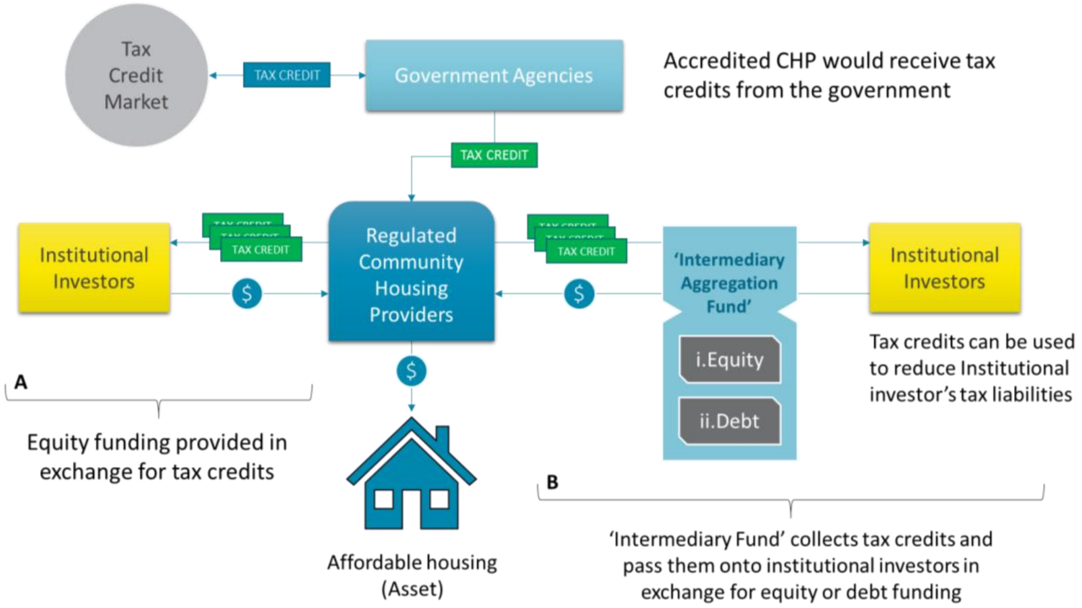
i. Equity financing – the 'intermediary aggregation fund' would assemble funds contributed by institutional investors and it would negotiate directly with housing developers to provide discounted upfront instalments (to fund affordable housing development) in exchange for a stream of tax credits for a fixed period (e.g. 10-years). Institutional investors would retain the ability to write-off these investments upon projection completion.

ii. Debt financing – the 'intermediary aggregation fund' could also offer financing options where it can provide debt financing for affordable housing development. For the CHPs, the loans would be serviced by a recurring stream of tax credits. Institutional investors could buy into the fund in return for these tax credits. Under this model, the project ownership would reside with the CHPs for the project to achieve GST exemption on the construction contract. A debt model has been structured by Minter Ellison specifically designed to deliver tax efficiency for institutional investors.[87]

[86] The role of this 'intermediary aggregation fund' could be served by institutional investors.

[87] An alternative to this debt financing model is to have the tax credits paid directly to non-profit registered CHPs as refundable tax offsets (RTO) in cash. This is because non-profit CHPs have no tax liability. This effectively is an operating subsidy for non-profit CHPs which expands their debt repayment capacity, hence giving them the ability to borrow more from NHFIC. Such arrangement removes the need to have institutional investors dealing directly with CHPs. Instead, institutional investor would indirectly finance affordable housing development by buying bonds issued by NHIFIC. However, this arrangement is not efficient as NHFIC loans require the borrower to achieve 1.5x interest coverage ratio (the net cash flow from the affordable housing project need to be 1.5 times the repayment).

Figure 25 – Construction funding via tradable tax credits



Source: ISA Analysis
Note: Bracket 'A' describes institutional investors liaising directly with accredited CHPs to finance their housing projects in exchange for tax credits. Bracket 'B' describes an 'intermediary aggregation fund' that acts as the middleman between CHPs and institutional investors. Financing under the latter scheme can be in the form of equity or debt.

An affordable housing tax credit scheme could be oversighted by the ATO with an emphasis on eliminating fraud and waste, ensuring that the scheme generates self-perpetuating funding towards the construction of affordable housing.

By embedding the Affordable Housing Tax Credit into the Income Tax Assessment Act, the scheme would serve to demonstrate how the alignment of policies and incentives could deliver benefits on multiple fronts – a greater supply of affordable housing (funded via higher levels of equity funding relative to debt) and lower taxes for institutional investors.

The tax-credit scheme for affordable housing was originated in the United States. The Low-Income Housing Tax Credit (LIHTC) program generated three million units from 1987 to 2015 in 45,900 projects and continues to this day, being made permanent in 1993. It now creates about 110,000 units a year (worth about $US8 billion). Operators achieved a 97.8 per cent occupancy rate in 2016 and a 0.7 per cent cumulative foreclosure rate. The scheme has a long, successful pedigree and high corporate investor confidence.

The Housing Capital Aggregator (private sector model)

The Housing Capital Aggregator (HCA) model has been developed by the Community Housing Industry Association (CHIA) to attract private institutional investors with longer investment horizons to invest passively into affordable rental dwellings managed by not-for-profit Community Housing Providers (CHPs).

The idea is to facilitate the pooling of large-scale equity funding to compliment debt funding sourced from NHFIC and/or commercial lenders at a project level. The workings of the model are shown in Figure 26, and the following is a brief outline of key features:

- A Managed Investment Trust (MIT) would be established to accept institutional capital.

- The MIT would allocate the aggregated capital to identified affordable housing rental projects already developed by the HCA. The affordable dwellings would be managed by not-for-profit CHPs.
- A combination of rental income and government subsidies would be used to pay back debt and provide distributions to equity investors.

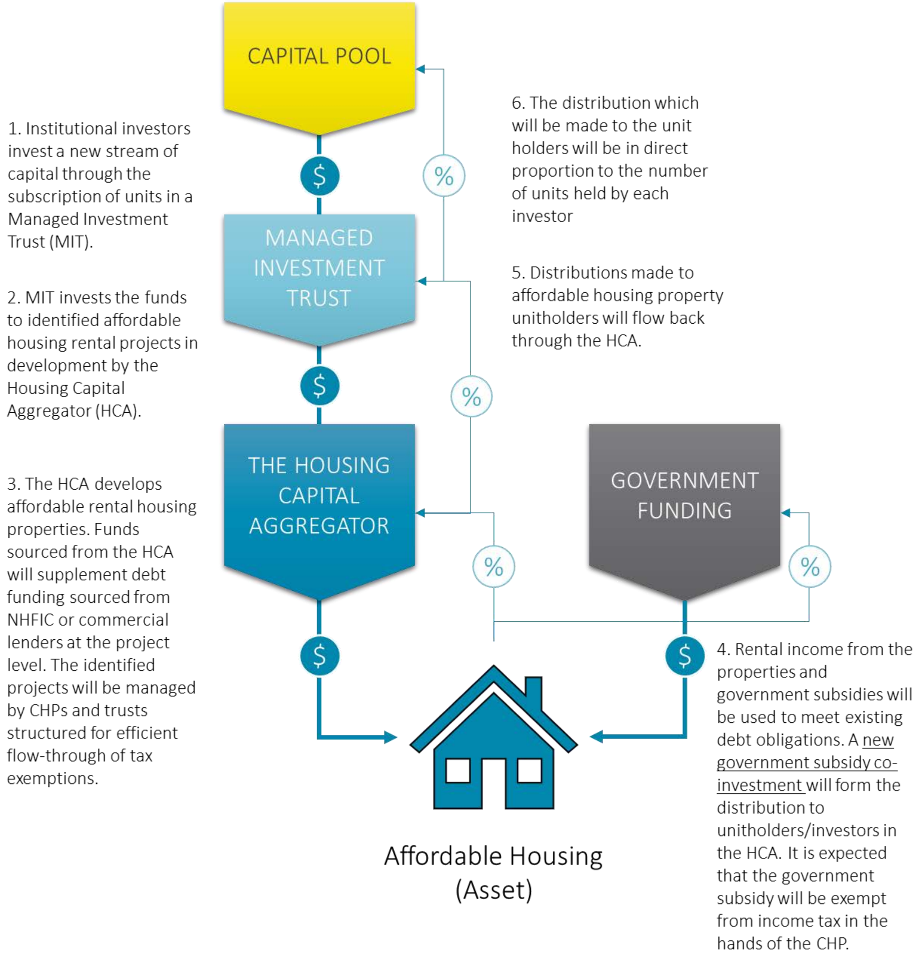
In order to guarantee enough cash flow to meet debt obligations and distributions to equity investors, the program requires the following:

- Commonwealth Rental Assist (CRA) for tenants; and
- **A new government subsidy/co-investment** – a source of funding for the distribution to unitholders/investors in the HCA (like our tax credit proposal above).

If the above government funding is secured, the proposed HCA would resolve risk and return concerns amongst institutional investors.[88]

[88] Community Housing Industry Association (CHIA) 2019, *Case for a Housing Capital Aggregator*, CHIA & The Constellation Project.

Figure 26 – The Housing Capital Aggregator



Source: Community Housing Industry Association

6.2 Policies to better support market efficiency in property markets

In this subsection, we examine existing policies and potential reforms that make it easier for households to upsize or downsize to the property that best suits their needs.

A central coordinating agency (Federal level)

We suggest there is a need for a coordinating agency in Australia that identifies where the need for affordable housing is greatest (in terms of local government area) by tracking house prices and rental yields (remembering that some regions are cheaper because they are more remote, rundown or less desirable).

The coordinating role properly belongs at the Federal level, with an office of national housing, perhaps operating within a central agency or independent authority, with more capacity to be guided by evidence-based analysis. The body would be charged with generating and releasing relevant analytics each year to the appropriate agencies within Federal and state departments and local councils and more broadly to the general public.

We also support the adoption of the United Kingdom's Letwin Report (2018) findings which suggest in the Australian context that state governments adopt new planning rules for large development sites which remove existing zoning restrictions provided they meet diversity objectives and giving local councils the authority to develop those properties via public corporations for later resale to developers.

Macro policy coordination to rebalance the supply / demand for affordable housing (Federal level)

We also suggest that broader monetary (especially prudential regulations) and fiscal policy (tax expenditures) are working across purposes to the overall goal of achieving affordable housing.

- In terms of fiscal policy, the Federal government and state and local governments could consider repurposing all or some of the pool of existing housing subsidies towards a single concession / program which more effectively targets the development and operation of new affordable housing.
- In terms of monetary policy, we suggest that the RBA adopt a broader policy target that captures both the impact of credit market innovation and a broad set of asset prices and nominal exchange rate movements, in addition to consumer prices. Either this or the RBA more effectively wield prudential policy to proactively smooth residential property prices.

Tax reforms including land tax (state level)

There are major tax reforms proposed in Australia which would support the stabilisation and efficiency of property markets in Australia.

Replacing the current stamp duty with a land tax would make switching properties more seamless and reduce frictions in the acquisition process – it would make upsizing or downsizing decisions much easier. Stamp duties are one of the most inefficient forms of taxation as they distort the investment decision making process with a significant upfront charge.[89] A land tax can be thought of as a second round of council rates, and are very efficient as they do not change buyer behaviour and are very difficult to evade. They also provide a recurrent rather than lumpy revenue stream for state governments which simplifies budget planning.

Replacing the company income tax with a corporate cashflow tax as proposed by Ross Garnaut would reduce land speculation and the use of leverage in the Australian economy and incentivise more productive business activity.[90]

A cash flow tax is identical to the existing company taxation arrangements, except that it:

- excludes all interest and finance related receipts and expenditures;[91]
- disallows depreciation expense; and makes all capital expenditure 100 per cent deductible upfront.

The justification for the cash-flow tax reform has three parts:

- it incentivises new investments;

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[89] Anthony, S. & Lu, G. 2017, 'Assisting Housing Affordability Discussion Paper', Industry Super Australia, Melbourne.

[90] Garnaut R., Emerson, C., Finighan, R. & Anthony, S. 2018, 'Replacing Corporate Income Tax with a Cash Flow Tax', *Melbourne Economic Forum*, December 2018. URL: https://www.industrysuper.com/media/replacing-corporate-income-tax-with-a-cash-flow-tax/

[91] Depreciation expenses and payments to related parties that aren't at arm's length are also disallowed. Exemptions are provided for banks to allow recognition of interest revenues and expenses.

- it addresses the imbalance in the tax system in favour of debt finance; and
- it broadens the tax base by encouraging wealthy taxpayers and foreign owned branch offices to pay their fair share of tax.

Part of the rationale for a cash-flow tax reform is predicated on linking some of the proceeds of the new tax to an explicit target for building new affordable homes for people on the high priority waiting lists across the nation via institutional investors accessing a tradeable tax credit scheme.

Audit of underutilised land (all levels)

The Federal government (especially the Department of Defence) and the state of NSW, with cooperation from the local governments, could instigate a data collection or review process which identifies underutilised land in regions where affordability pressures are the greatest.

Better use of existing vacant sites

This proposal is based on the understanding that there are significant publicly owned sites that are suitable for major residential developments – including prime inner-city sites with scope for affordable housing. Examples include disused manufacturing sites, golf courses, former housing commission developments, vacant space above municipal car parks and railway car parks, space around railway stations and disused siding and other land set aside for transportation activities. Many of these sites could be redeveloped and provide a funding source for a large expansion of affordable and social housing in the inner city.[92]

Upgrading density around train stations

High density developments around train stations make sense as workers no longer need to suffer from traffic congestion in their commute to and from work. The size of these developments (density and/or height) could be contingent on the provision of affordable rental housing, and these would be particularly suited for key workers such as nurses and law enforcement officers in the early stages of their careers where market rents may not be affordable.

6.3 Covid-19 and affordable housing

The Covid-19 pandemic raises the priority for dealing with affordable housing. In 2020, Australia is in-the-midst of the greatest global peacetime health and economic shock since the 1930s' depression. While the near-term economic challenges are not the focus of this paper, there are further challenges raised by the Covid-19 pandemic.

The impact from Covid-19 will be most serious for the poor. Their already precarious position makes it likely that negative shocks will have a knock-on effect that results in further cumulative losses (Coram and Anthony, forthcoming).

The full economic and other effects of Covid-19 is difficult to estimate at this stage but it has already cast light on the state of our housing system. Adequate housing is no longer just about providing the most vulnerable in our society with shelter, but it has become an essential part of the lockdown measures needed to keep people at home and contain the spread of the virus. People who are homeless and those living in overcrowded accommodation are among the high-risk groups, thus highlighting the need to address the matter with greater urgency.

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[92] Anthony, S. & Lu, G. 2017, 'Assisting Housing Affordability Discussion Paper', Industry Super Australia, Melbourne.

The pandemic reminds us yet again about the state of our housing inequality, which leads to vastly different outcomes in terms of physical and mental health, and abilities to work and study from home. People with secure housing and the right amenities are able to maintain physical distancing and it provides them with the ability to continue to work or study remotely. Those living in insecure housing, with short tenures, or are suffering from housing stress, can find it much more difficult to maintain overall wellbeing, not to mention the anxiety from eviction due to the loss of economic means to meet the cost of accommodation.[93]

We are seeing in many cases where people (many of them young adults) are moving back home or are forced to seek more affordable accommodation due to loss of income. In the latter, this means moving to perhaps more overcrowded homes, share houses or even becoming homeless or couch surfing, placing themselves and others in the house at higher risk of contagion.[94]

Homeless people are particularly vulnerable to infection and need to be adequately sheltered. The homeless often suffer from chronic health conditions and live in crowded circumstances without the ability to social distance.[95] Addressing the housing needs of the society's most vulnerable is important to keep them and the wider public safe and contain the spread of the virus.

The Covid-19 crisis provides the urgent justification to address the 30-year decline in affordable housing in NSW and more broadly as part of an effective and targeted fiscal stimulus package that addresses the needs of the disadvantaged. Unfortunately, once again, it seems that governments are still more inclined to help those who can afford to buy or renovate - at the expense of those with little or no capacity to buy.

6.4 **Boosting jobs and supporting economic recovery**

As the nation faces the onset of a double-digit unemployment rate, the Federal government has signalled its desire to ramp up infrastructure spending to kick-start the post-pandemic recovery phase. However, we believe one of the best ways to stimulate the economy and boost jobs and demand, is to invest in affordable housing construction.

There are several reasons why such investment would be beneficial:

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[93] The NSW Government has introduced measures to restrict landlords seeking to evict tenants due to rental arrears due to Covid-19. It includes a six-month restriction on evictions if the tenants are financially disadvantaged by Covid-19, unless they have first negotiated with the tenant a rent reduction.

[94] Raynor, K. Wiesel, I & Bentley, B. 2020, 'Why staying home during a pandemic can increase risk for some', Discussion Paper, Hallmark Research Initiative for Affordable Housing, The University of Melbourne. Website accessed 14/07/2020 URL: https://msd.unimelb.edu.au/atrium/why-staying-home-during-a-pandemic-can-increase-risk-for-some

[95] The NSW Government has funded hotel rooms for 30-days for those homeless people who are unable to maintain social distancing.

Cohen, H. & Mitchell S., 'From sleeping rough to four-star hotels: How coronavirus is changing our approach to homelessness', *ABC News*, 25 April 2020. Website accessed 14/07/2020 URL: https://www.abc.net.au/news/2020-04-25/homeless-put-up-in-four-star-hotel-during-coronavirus/12176942

- Affordable housing construction as a stimulus measure meets most of the principles outlined by The Australian Institute's *Design Principles for Fiscal Policy in a Pandemic*. These principles are[96]:
  - Go early: Timeliness of the stimulus is key;
  - Go hard: The size of the stimulus is important;
  - Go households: Put purchasing power with households who are more likely to spend it;
  - Target domestic production;
  - Target activities with high direct employment intensities;
  - Target those most impacted by the crisis;
  - Target useful projects that deliver co-benefits; and
  - Target regional disadvantage.

Higher levels of affordable housing construction not only meet domestic employment and production criteria outlined above, but also benefit sectors of the population with a higher propensity to consume. The provision of social housing also delivers health and wellbeing benefits, enabling tenants to study, work and contribute positively to the society.

- Building more affordable housing would boost the struggling construction sector that employs more than one million Australians and contributes around eight per cent of GDP.[97] A steady pipeline of affordable housing projects would guarantee jobs in the construction sector and help it weather the Covid-19 downturn. See ***Attachment A*** for a broader discussion of the economic benefits associated with affordable housing construction.[98]
- Such housing constructions also indirectly support businesses that provide goods and services to the construction industry. Any social housing stimulatory package needs to prioritise the procurement of local producers. This also provides the opportunity to apply new innovative and energy efficient building materials and technologies to reduce energy cost.

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[96] Denniss, R., Grudnoff, M., & Richardson, D. 2020, 'Design Principles for Fiscal Policy in a Pandemic', The Australian Institute, 20 April 2020. Website accessed 14/07/2020 URL: https://www.tai.org.au/content/design-principles-fiscal-policy-pandemic

[97] Raynor, K. Pert, A., Bentley, B., Crawford, R. & Wiesel I. 2020, 'Investing in Social Housing During a Pandemic', Pursuit, The University of Melbourne, 10 June 2020. Website accessed 14/07/2020 URL: https://pursuit.unimelb.edu.au/articles/investing-in-social-housing-during-a-pandemic

[98] A study of the housing procurement (EOI) scheme initiated by the Department of Housing WA in 2011 has found that based on the expenditure of $293 million to purchase 983 properties, the direct and indirect economic impact on the construction sector and other industries was $149 million and $210 million respectively. Another $106 million indirect effect from consumption was estimated. A total of 1,491 jobs were created, of which 427 are within the construction sector.

Conclusion

This discussion paper has sought to present evidence on the current affordable housing supply gap in NSW, the underlying issues with existing policies and how we need reform and innovate to close the affordable housing gap. As clearly stated by the Productivity Commission (2019), 'Australia's social housing system is broken'.

Policy mix

The housing shortages in NSW and rest of Australia could be addressed with the right combination of government policies and funding reprioritisation to attract equity from the private sector. Our suggestions offer a mix of responses that give policy makers flexibility to choose. The following lessons are key to the success of affordable housing development:

- A rational program mix needs to be achieved via a collective approach across jurisdictions.
- Enough and sustained government subsidy is critical to achieving scale housing developments.
- There is no 'silver bullet' – but a better mix of appropriate equity and debt funding schemes needs to be accompanied by macro and micro policy reforms to help mitigate the boom-bust property cycle.

For example, land provision is crucial to most affordable housing development commencements. Therefore, policies around identifying underutilisation of public sites and other efficiency measures to subsidise (or at least normalise) unimproved land values can dramatically improve the financial feasibility of projects.

A summary of the various funding models and indirect policies mentioned above, their impact on the budget, implementation instrument and level of government involvement are shown in Table 18.

Table 18 – Policy approaches

Equity incentives	Budget*	Instrument	Gov vs Private Provision
WA Integrated Development model	On budget	Multiple instruments	More government
Financial Corp. Fund	Off budget	Single instrument	More government
Tax Credit	On budget	Tradeable tax credit	Less government
Capital Aggregator	On budget	Multiple instruments	Less government
Efficiency measures	**Budget***	**Instrument**	**Gov vs Private Provision**
Oversight agency to identify shortages to guide planning	Departmental outlays	Transparent report of shortages via data collection	Federal government

Equity incentives	Budget*	Instrument	Gov vs Private Provision
Coordination of macro policy	Revenue neutral	Mix of monetary / prudential & fiscal pol.	Federal government
Tax reform (land tax)	Revenue neutral	Budget policy reprioritisation	All governments
Audit of underutilised land	Revenue positive	Data gathering and analysis	All governments

Source: ISA Analysis

*Note: *Within or outside general government P/L or balance sheet.*

Intergenerational poverty

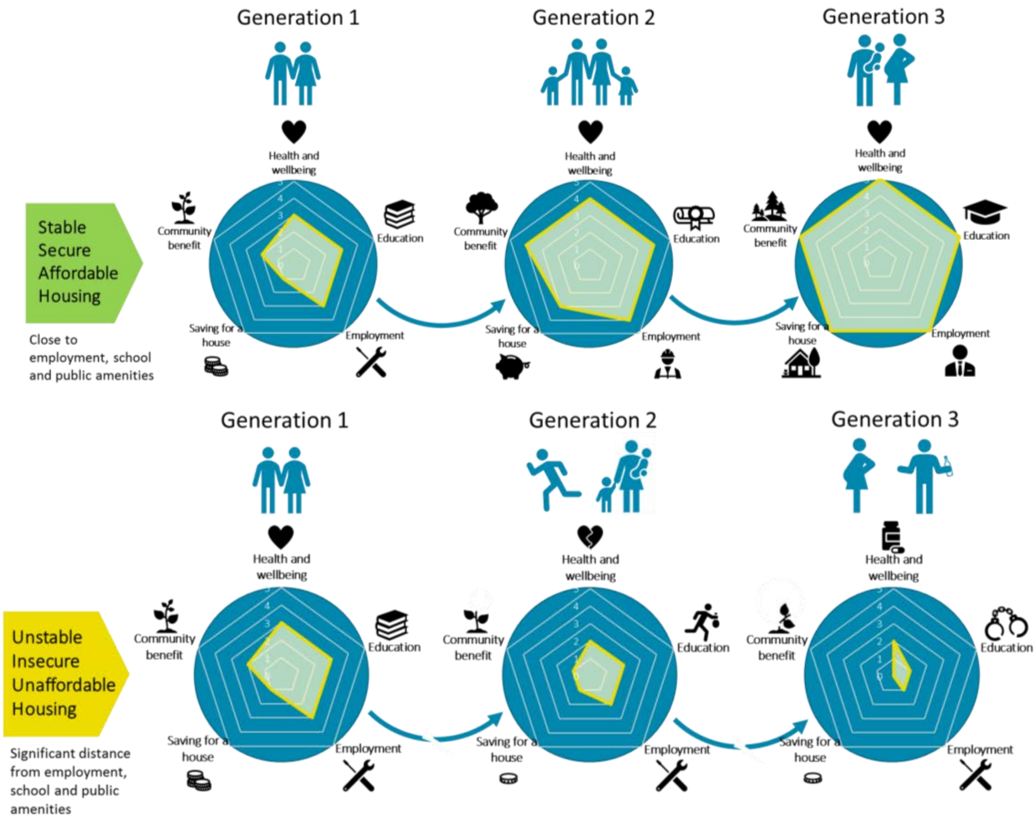
The lack of access to secure an affordable dwelling for the most vulnerable has profound social and economic consequences. The sad fact is that the precarious position of the poor makes it inevitable that a continual deterioration in their capacity to function in the economy is likely without the sort of stop loss mechanism provided by housing. In more concrete terms they are highly likely to suffer adverse impacts on things like educational outcomes, employment and earnings potential, family stability and health and wellbeing. All this results in an erosion of human capital which may be difficult to reverse.

Given the current affordable housing shortfalls and long public rental waiting list, the housing outcome produced by existing policy and funding measures are not enough. Of concern is the lack of new funding provision under NHHA and no forward commitment to new capital spending in government budgets, meaning growth in the social housing stock appears unlikely in the near future.[99] As payments for incentives under the NRAS scheme (in NSW) likely to be extinguished by the end of 2026, growth in social and affordable housing would need to come from CHPs and other private sources to meet the growing demand.

The failure to address the current supply shortfall not only affects a single lifetime but is likely to create conditions that persist through generations (Coram and Anthony, forthcoming). In many cases these conditions will progressively worsen. See Figure 27 for example.

[99] Community Housing Industry Council (CHIC) meeting, 18 December 2019.

Figure 27 – Intergenerational impact of insecure housing



Source: ISA Analysis

Bridging the affordable housing gap is possible through the collective efforts of governments, not-for-profit groups and the private sector. Key to this success is to establish a sustainable funding stream to support affordable housing development and operation. This requires a combination of policy reforms, government incentives and innovative funding models to attract and retain capital.

As explored in this paper, a better housing outcome would help put a stop loss on continual deterioration of human capital. It would bring both social and economic benefits to our cities in the form of improved family wellbeing, access to employment and public amenities and higher workforce productivity. The economic benefits that stem from ongoing construction activities and improvements in human capital (higher productivity, tax revenues, reduced demand on welfare and medical services) from bridging the affordable housing gap justifies the additional expenditures needed. The development of a sustainable and efficient affordable housing sector will certainly benefit generations to come.

Attachment A – Spill-over benefits from constructing affordable housing

In this attachment, we examine the economic benefits of government led, large-scale affordable housing construction in Western Australia (WA). The scheme shows how counter-cyclical, stimulatory investments such as affordable housing construction can have a positive impact on the construction industry and the wider economy.[100]

The scheme consisted of a large-scale, government led affordable housing procurement also known as the shared equity Expression of Interest (EOI) initiative by the WA Department of Housing. The EOI sought to procure 1,005 low-cost dwellings (by end of June 2013) at below market price which would be made available for affordable sales under a shared equity scheme.[101] The discounts achieved through the EOI would become the government's equity share in the property portfolio. Another benefit sought by the Housing Authority was to support employment and activities within the residential construction industry along with other indirect economic benefits to counter the construction industry downturn at the time.

The shared equity EOI also included the ShareStart loan, in which eligible applicants were able to obtain loans to purchase properties sourced under the EOI project. However, in this section, we will be focusing on presenting the short and long-term economic benefits from the additional construction activity brought by the EOI procurement.

To do this, we refer to the input-output modelling undertaken during the evaluation of the shared equity EOI scheme by AHURI and PricewaterhouseCoopers.[102] It is clear from the report that the procurement scheme led to increased economic activity as suppliers and contractors gear up to meet the demands from the construction industry. Construction contracts were also 'turnkey', meaning all homes are fully furnished before being sold to buyers, thus requiring additional materials such as carpets, blinds, TV antennas etc. Significant multiplier effects can be anticipated from a chain of contracts with builders, subcontractors, tradespeople, manufacturers and suppliers.

Short-term economic benefits

The report examined **five key elements** of wider economic benefit in the short-term as a result of the EOI procurement scheme (where the Department of Housing purchased 983 properties for $293 million):

- **The 'initial effect' or direct impact of the procurement scheme equated to $149 million**
  This amount was the direct additional activity created in the construction industry as a result of the EOI scheme.[103] One of the major benefits of the scheme was to stimulate residential construction activity amid an industry downturn. The scheme created new construction

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[100] Anti-cyclical investment refers to government stimulus spending during economic downturns with the aim of maintaining employment and demand.

[101] Thomson, M., Winter, I., Jones, K., Watson, R. & Dresser M. 2013, 'A new approach to delivering shared equity opportunities in Western Australia: a case study evaluation – Final report', AHURI & Pricewaterhouse Coopers.

[102] Given the widely acknowledge limitations of Input-Output analysis and particularly its susceptibility to over-stating impacts when an economy is close to full employment, the reporting of results is focused on the direct, first round impacts of the shared equity EOI on the residential construction industry and industry supply inputs into the construction process. *Ibid.*

[103] According to the report, 983 properties were purchased by the Department of Housing WA for $293 million. The market value of these properties was $338 million.

work that otherwise would not be there. This ensured continued activity, employment, cash flow and demand for goods and services for downstream businesses. Businesses accepted low profits in exchange for revenue and maintaining employment.

- **The 'first round effect' or the amount of output produced by construction industries as a result of the 'initial effect' – estimated to be $112 million**
  As construction activities pick-up, the demand for materials and services from suppliers increased as a result - we label this as the 'first round effect'. The largest supplier to the residential construction sector is construction services, followed by finance and insurance services, and structural metal product manufacturing.
- **The 'industry support effect' or the amount of output produced by all industries to support the 'first round effect' - $98 million estimated**
  The 'industry support effect' refers to the amount of additional economic activities generated in industries that supply the supplier industries for the construction sector. The amount was estimated to be $98 million.
- **The 'consumer spending effect' or the amount of additional output resulting from consumption from wages as a result of new construction activity - $106 million estimated**
  As the procurement scheme creates additional demand in the economy, the overall economy activity picks up and induces increased consumption through wages and salaries paid to labour and (potentially) investment returns to the owners of capital. This increase in consumption was estimated to be worth $106 million.
- **The 'employment effect' – 1,491 jobs estimated to be created directly and indirectly[104]**
  The additional $149 million worth construction activity supported 427 jobs directly in the construction industry and 664 jobs indirectly when the analysis is expanded to include industries that supply goods and services to the construction sector (first round effect).

In terms of the amount of economic output from the investment, a total of around $360 million (initial, first round and industry support effect) was driven by the $149 million initial construction activity – resulting in a multiplier of 2.4. When we combine the four effects – 'initial', 'first round', 'industrial support' and 'consumption', the total increase in economic activity due to the additional demand from the construction sector was estimated to be $466 million and the breakdown is shown in Table 19.[105]

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[104] The 1,491-jobs estimated via total multiplier effect need to be treated with caution due to the input-output assumptions. The total multiplier is likely to over-estimate the total impact on the economy in the absence of capacity constraints in the modelling.

[105] The $466 million worth of economic activity need to be interpreted carefully due to input-output assumptions. The total multiplier is likely to over-estimate the total impact on the economy in the absence of capacity constraints in the modelling.

Table 19 – Output multipliers

	Output multiplier	Value
Initial effect (direct)	1	$149,239,533
First round effect (indirect)	0.75	$111,929,650
Industrial support effect (indirect)	0.66	$98,498,092
Simple multiplier	2.41	$359,667,275
Consumption (indirect)		*$105,960,068*
Total multipliers	*3.12*	*$465,627,343*

Source: AHURI & Pricewaterhouse Coopers

Note: The 'total multiplier' should be interpreted with caution. Due to the input-output assumptions, this multiplier is likely to over-estimate the total impact on the economy in the absence of capacity constraints in the modelling.

It was estimated that the initial $149 million worth of construction activity directly supported 427 jobs in the construction industry and 664 jobs indirectly (as the result of 'first round' and 'industry support effects'). This amounted to the total of 1,092 jobs. However, if consumption or other effects are considered, then this would amount to a total of 1,491 jobs. The total employment generated from the project either directly or indirectly are shown in Table 20.

Table 20 – Employment multipliers

	Employment multipliers	Employment numbers
Initial effect (direct)	2.86	427
First round effect (indirect)	2.42	361
Industrial support effect (indirect)	2.03	303
Simple multiplier	7.32	1,092
Total multipliers	*9.99*	*1,491*

Source: AHURI & Pricewaterhouse Coopers

Note: Estimations of the impact on output and employment in the wider economy (the 'total multiplier') should be treated with caution and considered as an absolute upper limit to the range of likely impacts. Employment multipliers are factors of the initial direct output figure of 149 (scaled down from one-million).

Long-term economic benefits

Such procurement scheme may also deliver potentially long-term, qualitative benefits to the construction industry and the wider economy.

- Anti-cyclical investment supports economic activity and employment during the construction industry downturn. This ensures job-losses are minimised and skills and expertise preserved and developed to be ready for the next round of private sector demand.
- Partnership with the government on the EOI work has several benefits for the construction industry:

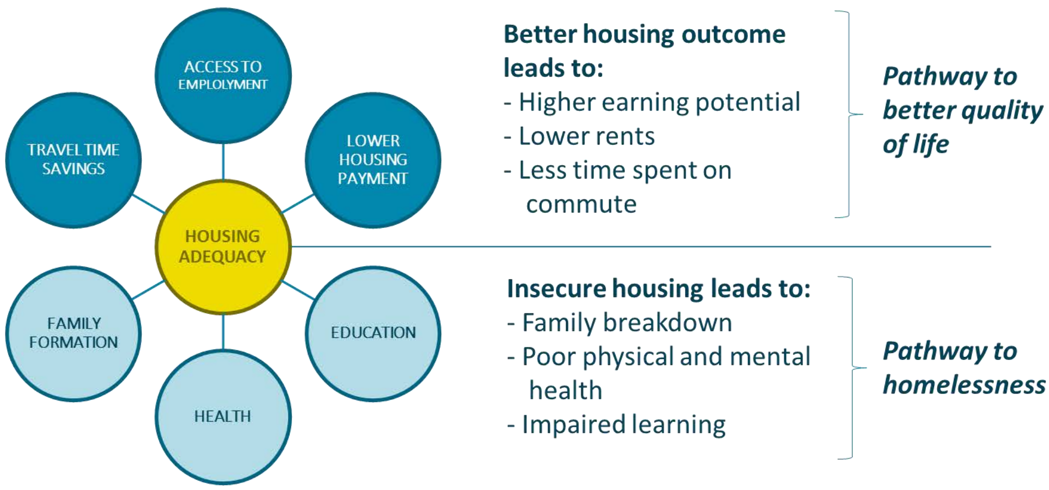
   - Capacity and skill building (training young appetencies, draftees, designers etc.) from working with large-scale government project;
   - Gaining exposure to the affordable housing segment – a new class of properties for some builders that has different requirements and specifications to private sales;
   - Formation of a new income stream (new business model) in the form of stable, low-risk government contract that would supplement a builder's revenue; and
   - Development of new construction techniques in the form of pre-built housing using production lines instead of traditional construction methods to further lower cost and reduce lead-time.
- Partnership with the government also delivers benefits to land developers as they're able to sell land that's difficult to sell to the private market, ensuring viability of the business in difficult times.
- Benefits to the household:
   - The scheme was able to deliver good quality house at an affordable price, with mortgage payment that are comparable to private rents. The shared equity scheme provided security of tenure, financial security, esteem and social status from home ownership.
   - Home ownership instead of renting allows the household to enjoy the benefits of asset price appreciation.

Attachment B – Measuring intergenerational and economic loss from insecure housing

In this section we analyse the links between housing and poverty in more detail. In Coram and Anthony (forthcoming), it will be shown that a major element in the dynamics of poverty is the cumulative nature of events that influence life chances. In crude terms if an agent starts with a low level of wealth, the chances of becoming destitute are very high without a stop loss barrier. It was suggested that housing operates in this manner. It is less clear how this works out in concrete terms.

In order to examine the details of these links we sketch out a methodology outlined in Maclennan *et al.* (2019) for identifying the productivity impacts from better housing outcomes (BHO).

Figure 28 – Productivity and intergenerational impacts from insecure housing



Source: ISA Analysis based on Maclennan (2019) & Nygaard (2019)

Immediate intergenerational impacts from insecure housing

Insecure housing adds stress to families and worsens their relationship, health and educational outcomes. Children are particularly vulnerable to such circumstances and frequent relocation and/or homelessness adversely impacts on their learning and behavioural development, resulting in losses in human capital and earnings potential.

A. Unstable family

The stress and uncertainty surrounding a lack of a secure home strains family relationships. The instability in tenure could be caused by the lack of affordability, family violence, low household income, illness or other factors. Also, individuals escaping domestic violence sometimes were unable to access affordable housing options. According to AIHW (2019), some 42 per cent of people assisted by specialist homelessness services had experienced family and domestic violence.[106] As a result, the public expenditure on dealing with domestic violence is on the rise and this is partly a consequence of financial hardship brought on by a lack of affordable housing.

B. Poor educational outcomes

The lack of stable, long-term housing also affects children's performance in schools. Unstable housing circumstances exacerbates family strains and is associated with greater truancy, behavioural problems and drop-out rates among children. Debates are still ongoing with regards to the causal relationships between housing instability and educational outcomes, and two explanations have been put forward so far:

- The financial stress from high housing cost results in material hardship for families and parents may not be able to afford schoolbooks, clothes and accessories to support their children's education.[107]
- Frequent relocation strains family relationships and school drop-out rates often increase after family breakups.[108]

While it is clear the investment in social and affordable housing may have a positive impact on children's educational outcomes by reducing family instability and financial hardship, the number of children that would directly benefit from better housing outcome is limited.[109] However, for those children who did benefit, the improvement in their level of wellbeing, educational attainment, employability and earnings potential is significant. This means their future incomes and purchasing power would be higher – directly benefiting their offspring. And it also means a high level of taxes paid instead of receiving social security. This is an example where better housing outcomes are linked to higher productivity and economic growth through better education and human capital accumulation.

C. Poor mental health

Insecure housing impacts on individuals' mental health and wellbeing, and in many cases health related circumstances paves the way into homelessness.[110] Housing affordability and uncertainty reduces households' sense of security and empowerment/control with the added stress of frequent relocations. Whilst the incidence of housing affordability and mental health indicators are strong, the causes of and recoveries from depression are complex and multifaceted.[111]

Mental health issues have both financial costs to individuals and the public, and for instances when it's occurring in families with children, it severely impacts a child's brain development,

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[106] Australian Institute of Health and Welfare 2019, *Family, domestic and sexual violence in Australia: continuing the national story,* Cat. No. FDV 3, Australian Institute of Health and Welfare, Canberra.

[107] Newman, S. & Holupka, S. 2014, 'Housing Affordability and Investments in Children', Journal of Housing Economics 24 (June).

[108] Evans, M., Kelly, J. & Wanner, R. 2009, 'Consequences of divorce for childhood education: Australia, Canada, and the USA: 1940-1990, Comparative Sociology.

[109] Nygaard, C. 2019, 'Social and Affordable Housing as Social Infrastructure – A literature review for the Community Housing Industry Association', Centre for Urban Transitions, Swinburne University of Technology, 7 November 2019, Website accessed 3/1/2020: https://www.communityhousing.com.au/wp-content/uploads/2019/11/Social-and-affordable-housing-as-social-infrastructure-FINAL.pdf?x33467

[110] *Ibid.*

[111] Handley, T., Rich, J., Lewin, T. & Kelly, B. 2019, 'The predictors of depression in a longitudinal cohort of community dwelling rural adults in Australia', Social Psychiatry and Psychiatric Epidemiology.

emotional regulation capacities and the ability to learn.[112] Early year intervention program (EYEP)[113] for the most vulnerable children in Australia has found mental health and relationship issues, family violence, alcohol and substance abuse as the most prevalent in families of child participants. The study also found that primary caregivers of children participating in the EYEP trial have higher levels of psychological distress. Poor mental health adversely impacts on the human capital of the individual, the wellbeing of their children and increases public expenditure on treatments and prevention.

Measuring productivity impact from Better Housing Outcomes

Improving the housing outcomes by providing secure, affordable and good quality housing for low income families would have a positive impact on their overall health and wellbeing. The provision of such housing at suitable localities shall be called 'Better Housing Outcomes' (BHO). According to Maclennan *et al.* (2019), BHO policies lead to affordable rental developments that provide safe neighbourhoods for families, close to employment and public amenities, lower rental payment, and its anti-cyclical nature (in investment and construction) potentially provides a boost to economic growth and productivity.

In this section, we take measurement on various attributes of BHO that would impact on broader productivity. Below, Table 21 provides a guide on what to measure when accessing BHO's impact on productivity. The scenario applies to major capital cities such as Sydney, and considers the following context:

- The concentration of jobs in or near inner-city areas;
- The severe lack of affordability of inner-city dwellings;
- Lower income households are forced to rent in low cost areas in the suburban fringes;
- This leads to long commute times to and from work; and

The current situation of residing in far-away urban fringes with poor access to employment and amenities is referred to as the Business as Usual (BAU) scenario.

[112] Tseng, Y.P., Jordan, B., Borland, J., Clancy, T., Coombs, N., Cotter, K., Hill, Alice. & Kennedy, A. 2017, 'Changing the Life Trajectories of Australia's Most Vulnerable Children', Report No.1, Participants in the Trial of the Early Years Education Program, Melbourne Institute of Applied Economic and Social Research.

[113] Early Years Education Program (EYEP) was provided by the Children's Protection Society (since its launch in 2010) and was intended to address the specific problems of vulnerable and at-risk children. The objective of EYEP is to ensure that the children who participate in the program arrive at school developmentally and educationally equal to their peers. The program has a dual focus: 1. Addressing the consequences of significant family stress on children's brain development; and 2. Redressing learning deficiencies. *Ibid.*

Table 21 – Measuring broader productivity impacts from BHO

Selecting locations for BAU and BHO

For **BAU localities**, we select areas (with low rent) where low to moderate income households typically reside. This can be selected using the SGS Rental Affordability Index for mid-2018 (SGS, November 2018). These areas are usually located near urban fringes and have poorer access to jobs and services.

For **BHO localities**, we select areas with high accessibility to jobs (usually within a 30-minute commute radius), good residential development potential and proximity to public amenities and employment opportunities.

Residential growth potential can be identified by measuring the area of mesh blocks that have been zoned as 'Residential' *less* areas currently occupied by existing dwellings or non-developable land.

Localities within 800m of a hospital are to be identified as areas meeting the criteria of proximity to public amenities/hubs.

We use Effective Job Density (EJD) measure developed by SGS as proxy for employment accessibility.

Having selected both BAU and BHO localities, we can use them for comparative purposes to identify the productivity advantages of BHO.

Item	Measuring the benefits from BHO	Note

1.

Travel time savings

Households would benefit from moving from BAU localities to BHO localities. To estimate the travel time savings:

- Identify where households would live in BAU and BHO localities.
- The reduction in average travel times (private and public travel modes) when households move to BHO localities.
- How the time savings are divided between work and leisure.

Transport for New South Wales (TfNSW) calculates that the value of time to each person travelling by either car or bus is $16.89 per hour.

The annual savings to worker from reduced commute time can be found by:

- Private travel time savings (hrs) x $16.89 = A
- Public travel time savings (hrs) x $16.89 = B
- A x (Modal split in BaU%) + B x (1 – Modal split in BaU%) = C (Annual savings per worker)

Assuming average 50% of travel time savings to be used for productive purposes, we multiply C by 0.5.

Note: Modal split refers to the proportion of time spent on private or public transport. Adding both proportions together equals 1.

2.

Greater access to labour market

Moving to BHO localities would enable greater access to a wider range of jobs, allowing workers to pick and choose the ones that best suits their skills. This contributes to higher productivity and economic growth as earning potential for workers rise and spending increases. We assume that the increase in earnings is a proxy for the 'agglomeration-induced' productivity boost from better skills matching.

To determine this increase in productivity, we compare the *differences* in annual earnings of BAU and BHO localities by:

- Qualification (bachelor and postgraduate, certificate, unqualified);
- Age (20-24, 25-29, 30-34, 35-39, 40-44, 45-49, 50-54, 55-59, 60-64); and
- Identify the population profile of households by qualification and age to give us weights to find the average annual earnings increase.

Note: Significant variation is present on the earnings boost between those with higher degree and those that are unqualified.

3.

Lower housing payment

Housing stress occurs when rent payment exceeds 30 per cent of annual income for those on lower income households. Any amounts higher would mean they have less money to spend on food, energy, transport, education and medical needs.

Lowering household's rental payment can improve the human capital accumulation through greater spending on transport and education.

We identify the savings that would occur by determining the excess rents (amount greater than 30 per cent of income) from renting in BAU localities. We call this 'overspend', and to determine the average annual value, we refer to ABS Census data to obtain the number of households by:

- Total household income (weekly); and
- Average annual rent.

The average overspend for each income bracket can be calculated by dividing the total dollars in the overspend range (where rent make up more than 30 per cent to 100 percent) by total households in this range.

By only selecting lowest to moderate income brackets, we then determine the average overspend on rent.

4.

Anti-cyclical investment

Whether anti-cyclical investment generates economic impact, the evidence was inconclusive. Some evidence can be found in reduced costs when investing during industry downturn as well as qualitative impacts of sector stability. However, the overall statistical evidence is not strong.

5.

Additional subsidy cost

Whilst achieve BHO delivers wide ranging productivity benefits, it also comes with higher costs from higher density housing in accessible locations. Hence it requires government subsidies to allow affordable rental to take place.

To identify the additional development cost of BHO dwellings, we measure the differences in land value, construction cost, provision of electrical, water and sewage, telecommunication and gas infrastructure, social infrastructure and others.

The government subsidy required would take into consideration the gap between market and affordable rents, the yield and/or return required by investors and how we finance the construction of the dwellings.

Source: Maclennan et al. (2019)

Attachment C – Monetising gains from adequate housing outcomes

In this attachment, we present study by Nygaard (2019) and examine quantitatively, the long-term cost of the failure to provide social and affordable housing as a basic infrastructure.

The inclusion of social and affordable housing as essential infrastructure to support economic growth has the potential to deliver positive outcomes (in dollar terms) for the health and wellbeing of low-income, disadvantaged individuals and families. It has been well established that housing stress or housing instability is associated with wide range of social problems such as homelessness, poor mental and physical health, substance abuse, loss of human capital, domestic violence and loss of family bonds.

Health and society costs

The inability to access social and affordable housing with integrated services by the homeless would incur significant health costs on the public. Transitioning the homeless into secure accommodation with adequate services would deliver a net saving to the taxpayer despite the cost of providing the housing accommodation and services. The paper also shows studies across NSW, VIC and WA that the provision of social and affordable housing to the homeless led to a reduction in hospital bed occupancy and lower levels of demand on emergency wards.[114]

The research undertaken by Nygaard offered two tentative conclusions on the wider social and economic impact of enabling access to social and affordable housing.

Table 22 - Health related expenditure savings (Australia average)

Access to social and affordable housing without additional tenant support.	Access to social and affordable housing with additional tenant support
The average estimated health expenditure reduction per annum from availability of social and affordable housing is assessed to range from \$500 in the 1st year to \$2,000 in the 4th year.	The average estimated health expenditure reduction per annum from availability of social and affordable housing is assessed to range from \$6,570 to \$13,270 depending on the precise group of people who are homeless or at risk of homeless that is considered.

Source: Nygaard (2019)

Note: Tenant support are additional tenant-specific services that address individual and community health, education, jobs-readiness, networking and social capital skills that play both a preventative and treatment role for individuals and communities. A caveat for the case study without tenant support is that the homeless population is not a representative sample of low and moderate-income households.

Estimated total cost to the public sector

The public sector would bear significant costs if actions are not taken to transition the homeless to social and affordable housing. The Australian Social Values Bank (ASVB) studied the total government expenditure savings that would occur if adequate accommodation for the homeless can be addressed. The estimated cost savings per dwelling to the society are listed in

[114] However, the sample size of the studies in NSW and VIC was small and therefore subject to greater variability.

Table 23 and Table 24 and are based on the construction of 100 social or affordable housing dwellings units.

The savings impact to society can be significant depending on the level of support provided to the homeless as they transition into social or secure housing.[115] Various studies were undertaken to identify the cost benefits to society and individuals (or households) as the homeless population are transitioned towards various forms of social and secure housing accompanied by support services. Based on the construction of 100 social or affordable housing, Table 23 shows by moving the homeless into secure housing, each dwelling is estimated to save the public sector $10,494 per year. The table also shows by offering the homeless tenant support – in the form of physical and mental health, community connection, etc., the savings on health cost would be $8,680 per year. These studies also provide an impact ratio for each of the six scenarios listed. The impact ratio[116] allows you to calculate the dollar impact on individuals based on the total society impact. Additionally, the studies show the ratio of dollar savings to the amount of government subsidy that maybe offered to a positively geared social or affordable housing development in middle-ring suburb in Sydney and Melbourne.[117]

[115] Secure housing is accommodation constructed by community housing organisations and is provided to homeless people along with mental and physical health support, assist with reducing social isolation and equip them to live successfully within the community (Mission Australia, 2012).

[116] Social & Economic Impact* ($) = Individual Impact ($) x (Impact Ratio x 100). *Total impact from 100 dwellings.

[117] The subsidy requirement is based on calculations by Nygaard (2019), that assumed subsidies cover 39% for affordable housing rental cost and according to the Affordable Housing Working Group (2016), subsidies cover 60% for social housing rental cost.

Table 23 – Savings from transition the homeless to social and secure housing

	Transition	Estimated total societal impact	Calculated individual impact	Impact ratio	Subsidy ratio AHSE	Subsidy ratio SHSE
			Per dwelling per year			
1.	Health cost savings to homelessness with regular homelessness support	$1,530	$1,530	1	8%	5%
2.	Health cost savings homelessness with tenant support	$8,680	$8,680	1	46%	30%
3.	Public sector total saving on homelessness to social housing	$5,699	$11,398	0.5	30.2%	19.4%
4.	Public sectors total saving on homelessness to secure housing	$10,494	$20,987	0.5	55.5%	35.8%
5.	Public sector total saving temporary accommodation to social housing	$2,626	$5,252	0.5	13.9%	8.9%
6.	Public sector total saving temporary accommodation to secure housing	$7,420	$14,841	0.5	39.3%	25.3%

Source: Nygaard (2019)

Note: Note: No.1 & 2 are estimates by Wood et al. (2016) and others. No. 3 – 6 are estimates based on calculations provided by the Australian Social Value Bank, and subsequently adjusted. The values used in these calculations are owned by the Alliance Social Enterprises. The values have been produced by Simetrica. These values are used under Licence #[P8Xw5y] with expiry date [7/11/2019]. Tenant support are additional tenant-specific services that address individual and community health, education, jobs-readiness, networking and social capital skills. The study was based on the construction of 100 affordable dwellings.

There are other benefits of providing social and affordable housing to the wider population beyond the homeless population. Although some of the societal savings are small, they nevertheless are worthy of discussion as they contribute positively to education and work outcomes. For example, Table 24 from Nygaard (2019) shows the individual impact from simply completing year 12 is $3,720. Overall, the completion of year 12 is associated with a 10-14 per cent increase in hourly earnings for women and men.[118] Other studies have also shown that as families secure social housing, a net 46 per cent of parents reported an improvement in subject performance and a net of 35 per cent reported higher level of motivation in their children.[119]

[118] Forbes, M., Barker, A. & Turner, S. 2010, 'The effects of education and health on wages and productivity', Productivity Commission Staff Working Paper, Melbourne.

[119] Phibbs, P. 2005, 'Housing assistance and non-shelter outcomes', AHURI Final Report No.74, Australian Housing and Urban Research Institute, Melbourne.

Table 24 – General savings from the provision of social housing

	Transition	Estimated total societal impact	Calculated individual impact	Impact ratio	Subsidy ratio AHSE	Subsidy ratio SHSE
		Per dwelling per year				
7.	Affordable rent (20% market discount)	$786	$786	1	4%	3%
8.	Improved education (Y12 completion) earnings increase	$372	$3,720	0.1	2%	1%
9.	Reduced personal spending on severe depression	$587	$14,670	0.04	3%	2%
10.	Reduced public spending on severe depression	$165	$4,130	0.04	1%	0.6%
11.	Reduced personal spending other depression	$279	$4,650	0.06	1.5%	1%
12.	Reduced public spending other depression	$73	$1,220	0.06	0.4%	0.3%

Source: No.7 is estimates by Nygaard (2019), No.8 is estimates by Ravi and Reinhardt (2011) and Applied Economics (2002), No.9-12 are estimates based on Hawthorne et al. (2003).

Note: The study was based on 100 the construction of 100 affordable dwellings.

Studies have shown that the provision of social or affordable housing for the homeless can have a positive impact on their overall welling and feelings of empowerment. Table 25 shows the monetised value of wellbeing impact of the homeless as they move from rough sleeping (and temporary accommodation) to social or secure housing.

Table 25 – Wellbeing impacts of transition to social or secure housing

Wellbeing outcome	Estimated total wellbeing value	Impact ratio
	Per dwelling per year	
Homelessness to social housing	$9,755	0.5
Homelessness to secure housing	$8,069	0.5
Temporary accommodation to social housing	$5,116	0.5
Temporary accommodation to secure housing	$3,431	0.5

Source: Nygaard (2019)

Note: These estimates are based on calculations provided the Australian Social Value Bank, and subsequently adjusted. The values used in these calculations are owned by the Alliance Social Enterprises. The values have been produced by Simetrica. These values are used under Licence #[P8Xw5y] with expiry date [7/11/2019]. The study was based on 100 the construction of 100 affordable dwellings.

Attachment D – Funding for the AHO and LAHC

In this attachment, we list tables that show detailed funding compositions for the AHO and LAHC (of NSW), in continuation from Table 13 and Table 14 of section 4.2.1. Total funding for the AHO was budgeted to be $149 million, with majority coming from 'Rental income' ($56 million), NHHA ($30 million) and NPARIH ($25 million).

Table 26 – Funding for the Aboriginal Housing Office (AHO)

($ million)	2019-20
NPARIH – Commonwealth (via DCJ)	25
NHHA – Commonwealth (via DCJ)	30
Grants from other Government agencies & SPP payments	16
Rental income (net off rebates)	56
Depreciation expenditure (non-cash)	21
Total funding	**149**
Less funding going to capital works	26
Total Recurrent Funding	**123**

Source: NSW Department of Communities and Justice

Total funding for LAHC was budgeted at $1,402 million, with majority sourced from 'Rental income' ($740 million), see Table 27.

Table 27 – Funding for the Land and Housing Corporation (LAHC)

($ million)	2019-20
Recovery Water charges	40
NHHA – Commonwealth & other recurrent grants (via DCJ)	89
Interest income	3
Rental income (net of rebates)	740
Management fee revenues	7
Depreciation	523
Total Funding	**1,402**

Source: NSW Department of Communities and Justice

Attachment E – Homeless persons in NSW over time

The following table compares rates of homelessness for years 2011 and 2016. The table is sourced from Productivity Commission Report on Government Services 2020 – Homelessness services. It clearly shows the rate of homelessness is on the rise in NSW.

Table 28 – The number of homeless persons per 10,000 of the population in NSW

	2011	2016
People who are in improvised dwellings, tents or sleeping out	2.8	3.5
People in supported accommodation for the homeless (b)	7.1	7.8
People staying temporarily with other households (c)	7.1	7.2
People staying in boarding houses	8.4	9.2
People in other temporary lodging	0.4	0.3
People living in 'severely' crowded dwellings (d)	14	22.5
Total homeless people	39.7	50.4

Source: Productivity Commission Report on Government Services 2020

Appendix F – Funding gaps for affordable housing

The following section outlines the assumptions and methodology used in the modelling of a typical 100-unit BtR housing in both inner-city and mid-outer suburbs of Sydney (see Section 3.3). The development will be financed via a mixture of equity and debt. The model allows for variations in the proportion of social, affordable and market rentals, and market sales to determine the level of recurring government funding/concessions required to achieve a target gross RoR.

Assumptions

The key assumptions and inputs into the BtR model are listed in Table 29 below. These values are applicable to metropolitan Sydney only. This example shows an 80/20 affordable/social rental mixture.

Table 29 – Major assumptions of the BtR model

	Scenario 1	Scenario 2		Scenario 1	Scenario 2
	Inner-city Sydney	Mid-outer Sydney		Inner-city Sydney	Mid-outer Sydney
Debt cost (bond aggregator)	4.00%	4.00%	Market rent vacancy rate (%)	3%	3%
Discount	1.25%	1.25%	Affordable rent vacancy rate (%)	3%	3%
Residual percentage of loan at end of term (%)	60%	60%	Social rent vacancy rate (%)	6%	6%
Dwelling cost			**Rental unit proportions**		
Market sale			Affordable rentals (%)		
1-bedroom ($ total)	$600,000 - $700,000	$450,000 - $500,000	Tier 1 (%)	80%	80%
2-bedroom ($ total)	$900,000 - $990,000	$550,000 - $650,000	Tier 2 (%)	0%	0%
3-bedroom ($ total)	$1,100,000 - $1,200,000	$700,000 - $800,000	Tier 3 (%)	0%	0%
Market rent			Social rentals (%)	20%	20%
1-bedroom ($ per week)	$500 - $600	$400 - $500	Total for rent (%)	100%	100%
2-bedroom ($ per week)	$700 - $800	$500 - $600			
3-bedroom ($ per week)	$800 - $850	$550 - $650	Affordable rentals ($)		
Dwelling types proportion			Tier 1 ($)	75%	75%
1-bedroom (%)	40%	40%	1-bedroom ($ per week)	$370 - $390	$300 - $340

	Scenario 1	Scenario 2		Scenario 1	Scenario 2
2-bedroom (%)	60%	60%	2-bedroom ($ per week)	$500 - $550	$350 - $400
3-bedroom (%)	0%	0%	Tier 2 ($)	60%	60%
			1-bedroom ($ per week)	$300 - $340	$250 - $280
Dwelling types (total no.)	100	100	2-bedroom ($ per week)	$400 - $450	$300 - $340
1-bedroom (no.)	40	40	Tier 3 ($)	50%	50%
2-bedroom (no.)	60	60	1-bedroom ($ per week)	$250 - $270	$200 - $240
3-bedroom (no.)	0	0	2-bedroom ($ per week)	$340 - $380	$240 - $280
Dwelling units gross floor space (sqm)			Social rent		
1-bedroom (sqm)	70 - 75	75 - 80	Social flat rent 1-bedroom	$120 - $130	$120 - $130
2-bedroom (sqm)	90 - 100	100 - 120	Social flat rent 2-bedroom	$170 - $180	$170 - $180
3-bedroom (sqm)	130 - 140	150 - 160	**Building costs**		
Development (CHP)			Estimated construction cost ($/sqm)	$2,700-$3,100	$2,400 - $3,000
Agency (CHP) cost ($)	$250,000 - $300,000	$250,000 - $300,001	Land area (sqm)	$2,500 - $2,800	$8,000 - $9,500
Agency (CHP) expected profit margin (%)	0%	0%	Land cost ($ per sqm)	$10,000 - $15,000	$2,500 - $3,000
Professional services cost ($)	$100,000 - $150,000	$100,000 - $150,001	Land premium (%)	0%	0%
Compliance & legal cost ($)	$100,000 - $150,000	$100,000 - $150,001	Construction duration (yrs)	2	2
Marketing cost ($)	$100,000 - $150,000	$100,000 - $150,001	Construction cost premium	0%	0%
Cost of construction - incl profit ($)	$20,000,000 - $30,000,000	$20,000,000 - $30,000,001	**Operation Phase**		
			CPI (%)	2.5%	2.5%
			Percentage rise in property value (%)	2.5%	2.5%
			Expenses per rental unit		
			Taxes	$0	$0
			Infrastructure charge (green field infra)	$1,000 - $1,500	$3,000 - $3,500
			Management cost (rental only)	$2,000 - $2,500	$2,000 - $2,500

	Scenario 1	Scenario 2		Scenario 1	Scenario 2
			Maintenance cost (all residents)	\$3,000 - \$3,500	\$3,000 - \$3,500
			Rates and insurance	\$3,000 - \$3,500	\$3,000 - \$3,500
			Land lease cost	\$0	\$0

Source: ISA Analysis

Note: Property values, rental costs and land values are presented in range form and serve as a guide only.

Methodology

The modelling of a typical 100-unit BtR development in Sydney has four main parts. In the first part, we need to establish the financing arrangements for the project construction. In the second part, we need to outline the costs of the construction phase. In the third part, we need to layout the forward 15-years' cash flow (after the 2-year construction period), or the operational phase of our BtR development. The final part of our modelling will involve solving for government funding (or funding gap) needed to achieve a gross RoR target.

Part 1 – Project financing

We first establish the metrics used for financing the construction of the BtR project. The construction will be finance via 70 per cent equity and 30 per cent debt. The cost of debt will be 2.75 per cent (after applying 1.25 per cent discount), and 40 per cent of the debt will be amortised during the 17-year term (2-year construction and 15-year operation). It is assumed that at the end of the 15-year operational phase, the housing development will be sold to new buyers at near market price.

Part 2 – Development and construction

We list expense items relating to the development and construction as shown Table 29, and assign costs to the first and second year of the construction. The construction cost will be split evenly in the first and second year, while development expenses such as legal, marketing, compliance, council charges and other professional service costs will incur in the first year. Land acquisition cost will also incur in the first year. A 10 per cent contingency allowance based on the total project cost has also been included.

After identifying project development and construction cash flows in the first and second year, we calculate the present value of these cash flows based on a yet to be determined discount rate. This rate will be explained in Part 4.

Part 3 – Operational phase

In this part, we've created a forward 15-year schedule of expected cash flows to identify the amount of government funding needed to achieve a gross RoR target. The main source of revenue would be in the form of rental income after considering 6 per cent vacancy rate for social rentals and 3 per cent vacancy rate for affordable rental. The other source of revenue will be government funding, which would be left as a variable to be determined later. On the expenses side, the main outgoings are management cost, maintenance, rates, insurance and loan repayments (based on 60 per cent residual at the end of the term). We assume no further expenses such as land and council taxes. The last major item in this schedule is the significant cash flow that would occur in year 17. This comes from the selling of the housing development to a new buyer at near market value. This cash flow will offset any outstanding debts to clear all liabilities at the end of the operational phase.

Like Part 2, the present value of each year's net operating income will need to be calculated based on a yet to be set discount rate.

Part 4 – Calculating the internal rate of return (IRR)

After setting up the present value of the initial investment (equity investment and other net cash flow) – let's call this the left side of our present value equation, and to have the present value of operational phase cash flow on the right side of the PV equation. The unknown variable would be the amount of government funding, which we need to solve to achieve a target RoR, which balances our equation. We manually input this rate and use a spreadsheet package to solve for the funding amount.

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Industry Super Australia

Melbourne

Casselden Place
Level 39, 2 Lonsdale St,
Melbourne, VIC 3000
P: (03) 9923 7131

Canberra

Dialogue
GF, 4 National Circuit
Barton, ACT 2600
P: (02) 6269 5710

@IndustrySuper

admin@industrysuper.com