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Involving the Private Sector in Affordable Housing Provision: Can Australia Learn from the United Kingdom?

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ABSTRACT *The focus of this article is to clarify the preconditions for the successful leverage of private investment to help both maintain and expand the affordable housing stock in Australia. To do this we examine a range of initiatives that have enabled such leverage in the UK and explore the lessons that can be drawn for Australia from this experience. The article provides an overview of UK experience since the 1980s and, from this, identifies the key factors that have both contributed to and constrained the expansion of affordable housing in the UK. It signals the key barriers and emerging challenges for the continued operation of this system of affordable housing provision in the UK and draws out the lessons, both positive and negative, that might help determine what is needed in Australia in order to fulfil the stated objective of the current Commonwealth State Housing Agreement—namely, to attract significant private investment into the provision of affordable housing. The concluding section addressing what might be done to increase the potential for leverage in the Australian situation, in the context of this policy goal.*

KEY WORDS: Affordable housing, private investment, housing subsidies, housing policy

1. Introduction

In 2003, the current Commonwealth State Housing Agreement (CSHA), authorised under the Housing Assistance Act 1996, came into operation in Australia. A number of principles guided the development of this Agreement.[1] Guiding principle number six, which committed the Commonwealth and States "to promote innovative approaches to leverage additional resources into Social Housing, through community, private sector and other partnerships", indicates one avenue by which this is to be achieved. This principle provides the motivation for this article.

The focus of this article is to clarify the preconditions for successful leverage, to help both maintain and expand the affordable housing stock. To do this we examine a range of

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initiatives that have enabled such leverage in the UK and ask what lessons can be drawn for Australia from this experience.[2]

Of particular relevance to this discussion is what is meant by ‘Social Housing’ in the context of the CSHA. Since the Agreement came into force this requirement has resulted in a broadening of the definition of social housing to incorporate a range of affordable housing options. A broad consensus has emerged amongst various stakeholders that affordable housing now covers any forms of government assisted or privately provided housing that can specifically assist households “at risk in the housing market” or “households who cannot compete successfully in their local housing market” to attain and pay for housing without experiencing undue financial hardship (Milligan, 2005).

The focus on ‘community, private sector and other partnerships’ provides an indication of the ways in which additional resources can be levered into social or affordable housing on the back of public assets or subsidy. This article focuses on understanding some of the factors likely to facilitate or impede the success of such an objective. When there has been a history of leverage, this understanding can be generated from past experience. However, when there is little experience to go on, more salutory lessons may be learned by looking further afield for cases where there has been more success. This article uses the fact that experience in Australia is so limited as a rationale for looking elsewhere for a more comprehensive set of factors that will need to be put in place if the 2003 CSHA is to meet its stated objectives. In particular, it looks to the UK because of its history of treating housing as part of the social contract involving large scale direct provision of affordable housing and because of its 20–30 year history of involving private finance in this provision.

The choice of the UK as a benchmark was made for a number of reasons. The first, pragmatic, one is that there is a readily accessible body of English language literature which can be used to inform the comparison. More fundamentally, the financial systems in the UK and Australia are similar and were liberalised at roughly the same time; housing is provided in broadly the same forms (although there are important differences in the relative importance of different tenures); the instruments by which housing assistance is provided are at least familiar;[3] and the legal, regulatory and land use planning frameworks in the UK have enough in common for meaningful comparisons to be made. Most importantly, the UK is seen as having had considerable success in levering private resources into the provision of affordable housing through a broad range of initiatives involving debt instruments, individual equity and land values.

However, it should also be noted that the introduction of private finance, by itself, is unlikely to solve the challenge of providing an adequate overall supply of affordable housing in countries like Australia and the UK. Indeed, in the latter, over the period in question, the total affordable stock fell.[4] What is clear, nevertheless, is that the decline in total social housing experienced in the UK would have been considerably greater in the absence of private finance. The importance of guiding principle 6 in the Australian context is that it calls for the mobilisation of resources for affordable housing that would otherwise not be forthcoming in the predominantly neo-liberal political climate that has imposed significant constraints on public expenditure. Meeting the broader challenge of matching the supply of affordable housing to the expanding need,[5] following a period of declining housing affordability, would require a substantial resource and policy commitment by government, particularly at the national level, and lies beyond the scope of this article.

Section 2 provides an overview of UK experience since the 1980s and, from this, identifies the key factors that have both contributed to and constrained the expansion of affordable housing in the UK. It also signals the key barriers and emerging challenges for the continued operation of the system of affordable housing provision. Section 3 draws out the lessons, both positive and negative, from UK experience that might help determine what is needed in Australia in order to fulfil the objectives of the CSHA. Finally there is a short concluding section addressing what might be done to increase the potential for leverage.

2. Affordable Housing Developments in the United Kingdom

Private finance has successfully been introduced into the provision of social and affordable housing in the UK by a complex mix of arrangements for the construction of new affordable housing and the transfer of existing stock from the local authority (LA) sector both to the housing association (HA) sector and to owner-occupation. The intervention of private finance has been a means of increasing private contributions through equity, rent and mortgage payments with the help of subsidy and 'stretching' the supply-side subsidies available so that they can meet a larger proportion of unmet need through the social housing sector.

Traditionally, affordable housing in the UK had primarily been provided through the LA sector—to the point where, in 1980, LAs owned around 5.4 million units—over 30 per cent of the total housing stock. Over the past 20 years the overall policy direction of the UK central government has been to reshape the social housing sector by limiting the public housing role of LAs in favour of building a viable HA sector, to encourage the growth of owner-occupation and to target supply subsidies in such a way that private financial institutions are prepared to provide additional finance.

The Initiatives

By and large, this policy direction has been a bipartisan approach, at least in England. Four key initiatives can be identified: the Right to Buy and the Large Scale Voluntary Transfer (LSVT) programs (which apply to the existing social stock) have been the drivers of the reshaping of the social sector; bringing in both debt and, in the case of owner-occupation, equity finance and enabling mixed public/private funding and the use of the land use planning system have enabled the provision of new affordable housing. These key initiatives are described briefly below. Berry *et al.* (2004) provide supporting detail. The discussion is focused upon England. The other countries in the UK, Northern Ireland (NI), Scotland (S) and Wales (W) have both similar and different policies in place.

Initiatives with respect to existing social rented housing. The 'Right to Buy' legislation has resulted in the (often highly) subsidised purchase of nearly 2 million homes by sitting LA tenants (Munro *et al.*, 2005). In addition homeownership has been extended through the introduction of several 'shared equity'-type schemes involving HAs as the 'partner' with the potential owner-occupier. These schemes, which are dependent on Social Housing Grant (SHG),[6] private mortgage finance and resident equity, are aimed at particular groups including social tenants and 'key workers' and, in total have delivered around 100 000 dwellings (for a review, see HC, 2003).

The 'Large Scale Voluntary Transfer' program was developed from earlier unsuccessful attempts at restructuring ownership of social housing. Cowan and Marsh (2001) provide a useful discussion of the origins of stock transfer. The transfer process is accomplished through the equivalent of a 100 per cent debt financed management buy-out, enabling the substitution of private for public funding (ODPM 2002). The transfer price is determined by government and takes into account the potential income stream (including the impact of Right to Buy), projected running costs and the investment needed to bring the stock up to a decent standard. Early transfers were in relatively high priced areas. However, over time the program has come to include negatively valued housing estates where a dowry (in the form of a capital grant) must be provided by central government to ensure transfers are financially viable. These transfers have been accompanied by initiatives to improve the management of both housing assets and the surrounding infrastructure in these estates (Gibb & Maclennan, 2003; Pawson, 2004). So far the program has resulted in the transfer of almost 1 million homes from LAs to HAs.

Initiatives with respect to new affordable housing. The capacity to attract private finance to transfer the existing stock in this way clearly depended on setting an acceptable price. It was also assisted by the successful introduction of mixed funding into the provision of new HA homes, starting in the mid 1980s (Whitehead, 1999). This was accomplished by providing capital grants (technically in the form of a subordinated loan) and freeing the HAs from traditional rent controls. In addition, depending on their household circumstances, all low income tenants are eligible for a government Housing Benefit (HB) payment up to their total rent.

Attracting funders also depended on the regulatory framework set in place by an already existing government agency, the Housing Corporation (HC), which also allocates the central government grants.[7] This provided the comfort necessary to attract a substantial flow of private mortgage finance into the HA sector to fund expansion. Private loans now typically fund about 50 per cent of HA acquisitions (that is, new building and renovations) and interest rates reflect the low risks associated with the sector (Wilcox & Williams, 2001). To date, over £35 billion has been invested by the lending institutions in the HA sector, of which more than 40 per cent has funded stock transfers (HC & NHF, 2005a for England supplemented by additional data drawn from NI, S and W). The remainder has funded provision of affordable homes (both rented and shared equity) through the HAs.

Finally, through Section 106 (S106) of the 1990 Town and Country Planning Act, LAs have been given the power to require residential developers to ensure a proportion of their units are affordable—either in the form of social rented housing or low cost homeownership and below market rentals. These properties are then generally owned and allocated by partner HAs. In most cases the affordable dwellings are provided on the site in question, though the contribution may be provided at other sites or, when acceptable to LAs, through a financial contribution (Crook *et al.*, 2002; GLA, 2004). In 2002–2003 the total number of affordable dwellings provided through S106 agreements was about 12 500, implying an average affordable housing contribution on larger sites of perhaps 10 per cent of the dwellings (Monk *et al.*, 2005). This proportion is expected to increase as the system evolves and is better understood by the key agents.

The Key Drivers

A large part of the housing policy story in the UK can be attributed to the increasing role of private finance. This raises the obvious question of why financial institutions have been so active in this sector over the past 20 years. The overview of key features of the British situation provided above suggests several answers.

Accumulated wealth. The first is that previous government policy had resulted in the accumulation of very significant housing wealth in the hands of the state. By the early 1980s, almost a third of the total housing stock was owned by LAs. This allowed government the option of transferring dwellings to sitting tenants and HAs at subsidised rates and, in the process, shifting the liability for future maintenance and renovation to the new owners (Whitehead *et al.*, 2005a). With an asset 'freed' from direct government controls and access to both demand- and supply-side subsidies, the new owners had both the capacity and the incentive to access private finance. This was not possible for LAs because of the tight constraints imposed by central government, on borrowing and rent determination.

Financial framework. The funding was available because, from the 1980s onwards, financial markets were progressively deregulated and liberalised, in line with international trends. Competition in financial markets encouraged the introduction of new products, especially in the residential mortgage area. Mortgage lenders had both the capacity and incentive to lend to social housing providers and Right to Buy clients, both of whom had adequate asset cover.

Moreover, given both the extent of the asset cushion and the government's preparedness to allow rents to rise, the finance market was given time to mature, moving from initially high margins and modest leverage in a new market to generating near risk free interest rates and around 50 per cent leverage as the market matured (Whitehead, 1999; Wilcox & Williams, 2001).

Regulation and management. Institutional preparedness to lend was enhanced by the creation of a strong supporting regulatory regime. In England the Housing Corporation introduced effective monitoring and reporting requirements and put in place procedures for identifying and rescuing HAs in financial or operational difficulties. By replacing what had been a bureaucratically organised regulatory system with one that better met the market needs of private lenders, policy makers overcame a major barrier to large scale investment in the affordable housing sector. The relatively stable environment of the 1990s, and the dependability of HAs in meeting their loan repayments,[8] reinforced the confidence of investors in the efficacy of the regulatory framework.

Further, the increasing dependence of the HAs on private investors fed pressures for more professional management and the application of commercial principles in the sector. Efficiency gains were sought through mergers among smaller HAs. These trends towards greater professionalism and industry concentration were reinforced by the regulatory and accounting systems and subsidy regime. The growth of large HAs and the emergence of syndicates of HAs also provided a new market for corporate bond sellers, ushering in further leverage opportunities and competitive downward pressures on the cost of finance. The lack of relevant expertise, in both the social housing and financial sectors, was addressed both through professional training and the recruitment of appropriate expertise from other industries (Bromwich *et al.*, 1991; Pryke & Whitehead, 1993, 1995).

In the context of capturing land value to make new housing affordable, the existence of a land use planning system which located the property rights with the UK government made it simple to empower local government to mandate the provision of affordable housing as a condition for development permission. Even so, much of this development requires additional subsidy in the form of SHG (Crook & Whitehead, 2002; Crook *et al.*, 2002).

Subsidies. In the case of stock transfers, viability was assured by a favourable transfer price and a commitment to providing the implicit subsidies for its upgrading within a broader community regeneration framework (Gibb & Maclennan, 2003; Pawson, 2004). This substantially reduced the perceived risk to investors, encouraging investment flows and shaving its cost. In the owner-occupied sector large discounts and conservative valuations similarly limited the risk of lending to lower income households.

Finally—and critically—the existence of HB and SHG has substantially limited the risks faced by lenders. As a mature, well-regulated finance market, both lenders and borrowers seem comfortable with the system of provision that has emerged. As a relatively low risk market, borrowing costs have fallen to less than 40 basis points (i.e. 0.4 per cent) above the inter-bank loan rate and funding is readily available.

These various components of British housing policy are complementary. The regulatory framework, payment of HB and the availability of upfront capital grants in the form of SHG together with the use of S106 powers together have provided an investment climate conducive to large scale engagement by both private mortgage lenders and equity investors. The partnership approach involved in many of these initiatives also tends to support central government urban regeneration strategies. Affordable dwellings provided through S106 agreements have enabled affordable housing to be located in higher land value ‘brownfield’ areas than occurs with conventional HA developments and, as a result, has helped to engender an element of ‘social mix’ (Monk *et al.*, 2005; Whitehead *et al.*, 2005b).

Most fundamentally, in order to make housing affordable, subsidy flows are delivered on both the demand and supply sides, while land availability is achieved through mandatory requirements imposed by the planning system. Equally, much of the subsidy involved, which has provided the comfort of unencumbered assets both for LSVTs and Right to Buy, has been in the form of the transfer of unrealised capital gains which has made it far more acceptable to the Treasury, because there is no overt subsidy in terms of Treasury accounting principles.

Emerging Challenges

There are a number of emerging issues that may challenge the continued operation of the system of affordable housing provision as it has developed in the UK. These relate to increasing risks and uncertainties arising from market, regulatory and policy change.

Market risks. Within housing markets, there is the risk that increasing competition from other tenures together with regulatory constraints on HAs may lead to inadequate returns for investors in lower demand areas where property values and market rents lag behind average or anticipated growth rates (Bramley & Pawson, 2002; Solomou *et al.*, 2005). This is particularly true in the context of some large urban LSVTs where declining demand could lead to major cutbacks in revenue and a fall in the value of underlying property assets.

Within financial markets the continuing consolidation of the financial services sector, through mergers and acquisitions, is reducing the number of lending organisations and introduces the risk that there will be reduced choices available to borrowing HAs. A smaller number of larger lenders may each reach their exposure limits to the sector—the maximum proportion of their loans devoted to a particular market (though this seems a distant prospect at present).

There are also risks with respect to funding availability: under Basel 2, the new financial regime to be established by the Bank of International Settlements by 2007, banks will have to make tighter risk based assessments of the different market opportunities and may seek to wind back or constrain their exposure to low risk–low return markets like the financing of affordable housing. The most likely outcome is that banks will have an added incentive to price risk more carefully, resulting in far greater differentials in borrowing costs than have yet been seen across the HA sector.

Policy risks. Recent and mooted changes in the rent-setting regime imposed on the HAs will see rents determined more in line with average local property values and incomes, rather than, as in the past, on the basis of development costs with an element of cost pooling. This will change the pattern of rents across the country and the risk profile of the stock for investors.

A similar uncertainty surrounds the future of the HB system. The government has introduced pilot programs in some areas in which they pay HB to private tenants based on the average rents in the area for the type of dwelling they are deemed to require and which are expected to be extended to all tenants across the country (Department of Work and Pensions, 2003). The uncertainty raised by changing a well-understood albeit flawed safety net may cause investors to re-think the current scale of their exposure to the sector. Without doubt, whatever the weaknesses of the current HB system the 'certainty' of payment is a key factor for funders. The proposed policy of linking HB to local average market rents may also push rents up for some tenants, private and social, in some high-value areas, reducing affordability and effective choice. More generally, private investors face the ever-present political risk of governments changing future arrangements around rent setting and subsidies, the regulatory system and taxation regimes, all of which would impact on the risk of lending to HAs and also, in some cases, to private developers contributing towards affordable housing under S106 agreements. The many debates and developments now in play threaten both revenue streams and the stability of the current regulatory environment, increasing uncertainties and risks that may influence the future commitment of private investors to affordable housing markets.

Uncertainties. Private funding initiatives in affordable rented housing have so far been focused almost entirely on debt. In spite of some attempts by government to stimulate private equity investment in rental housing (see Crook & Kemp, 1999), equity investors continue to avoid this market. The UK government's current emphasis on Real Estate Investment Trusts (REITS) may provide a way forward for bringing in private equity to rented housing but would require additional restructuring in the social sector before such an instrument could be successfully introduced (Ball & Glascock, 2005). Similarly extending SHG to developers has some potential but the private involvement may be short term (HC, 2004).[9]

The second area where additional equity could be levered in is in the context of low cost homeownership and it is in this area that current policy initiatives are being concentrated—although again the initial lead source of funding will be debt finance (Hoyle, 2004; Whitehead & Yates, 2005). The government has suggested that existing schemes should be restructured to increase the leverage of private funds though equity sharing loans in part underwritten by private financiers accepting an equity interest in these homes. In addition Social Homebuy—a highly modified version of the Right to Buy—potentially enables the further recycling of social assets to support partial homeownership across income groups (ODPM, 2005a, b).

3. Are there Lessons for Australia from the UK Experiences?

Whether these experiences in the UK can provide lessons for Australia depends largely on similarities and differences in the institutional, regulatory and financial frameworks in which each country operates. We start with the negatives by examining why it will be more difficult in Australia and then turn to the opportunities by examining how existing assets and powers can be better used to expand provision.

Possible Constraining Factors

In what follows, it is assumed that the issues arising from the ownership and funding of State Housing Authorities (SHA) stock in Australia are broadly similar to those arising from LA owned stock in the UK. Likewise, it is assumed that the community housing providers in Australia have the potential to operate in the same way as HAs in the UK.

However, there are a number of key differences in the way in which social or affordable housing is provided in the UK which are likely to limit the extent to which the initiatives discussed above can be transferred to Australia. These relate to the size of the social housing sector and, more broadly, differences in tenure structure between the two countries, to the structure of housing benefit, the existence of a strong regulatory framework, the property rights framework that underpins the planning system and, not unrelated to this last factor, to differences arising from a unitary compared with a federal system.

Institutional differences. The first difference relates to the size of the social housing sector which, in Australia, accounts for as little as 5 per cent of the total housing stock. The small size of this social housing sector, and its effective targeting on the most disadvantaged sections of the population, militates against the chances of using the dominant vehicles adopted in the UK over the past two decades to transfer stock out of LA ownership to owner-occupation or independent social landlords. Targeting means existing tenants of both providers of social housing in Australia generally are unable to generate sufficient rental income to even cover operating costs, let alone enough to enter into homeownership or to generate the required rates of return of private investors.

In addition, because of its small size and lack of financial management skills, the community housing sector currently is poorly placed to take over management through stock transfer from the SHAs. This suggests either that new forms of independent social landlords might have to be developed to manage not just the housing stock but also the restructuring of land and other capital assets, or that the initiatives might have to be undertaken by the SHA themselves.

This need for new forms of social landlords was also true in the UK. It was addressed through management buy-outs by the housing departments of the LAs, although the new landlords followed the existing HA model and were subject to the existing regulatory body (Whitehead, 1999). The recent development in the UK of Arm's Length Management Organisations or ALMOs also offers some useful pointers to Australian policy makers (CIH, 2005). A form of ALMO might allow SHAs to 'hive off' the stock to new business units, initially staffed by their own housing officials. This could provide a base on which to extract accumulated value in the public stock, valued at over $30 billion, in order to grow the social housing sector, as has occurred in the UK.

Differences in scale and scope of subsidies. A second major difference between the two countries is in the scale and scope of the housing subsidy arrangements. Both before and after restructuring in the UK, significant amounts of supply and demand subsidies have been provided and continue to be provided to social housing.

This is not the case in Australia. Capital subsidies delivered through the CSHA have fallen in real terms and are governed neither by movements in housing costs nor by any assessments of unmet housing need. As importantly, rents charged by the SHAs are tied to the income levels of tenants. One unintended and undesirable consequence of the policy of targeting public housing to the most disadvantaged is that, as indicated above, the revenue base of the SHAs has grown more slowly than their costs, throwing these agencies into financial operating deficits and removing their capacity to use their asset base to increase the supply of affordable housing to meet the burgeoning need (Hall & Berry, 2004). Currently, unlike the UK, there is no mechanism to ensure that there are sufficient subsidies to meet the gap between what tenants can afford to pay and what it costs to provide their housing. Past research in Australia has suggested that, without such subsidies, there is little likelihood of funding social housing from similar sources of private finance to those that have been involved in the UK (Berry, 2002; Allen Consulting Group, 2003).

As a result, to ensure an adequate revenue stream to enable the leverage of private funds it is necessary to separate the rental stream from the incomes of specific tenants, to provide subsidy for the poorest or to change the client mix (which would mean that the goal of housing those in the greatest hardship is lost).

Regulation. The third difference arises simply from the fact that, over a 20-year period, the UK has seen the maturation of a robust and successful regulatory framework that has supported the growth of what might be judged a modestly efficient HA sector and has provided the necessary comfort to private investors, enabling them to finance that growth (HC & NHF, 2005b). It is only in the past few years that capacity-building within Australia's community housing sector has emerged as a serious possibility but, in the absence of opportunities to put them into practice, their financial management skills are still rudimentary (as indeed they were in the HA sector in the UK in 1988, Pryke & Whitehead, 1993, 1995).

As yet in Australia, no progress has been made on the establishment of a single regulatory system or agency, such as the Housing Corporation, that would provide the monitoring, audit and rescue functions necessary to support efficient operation and attract large volumes of private investment. In states like Victoria that are looking towards an expanded role for HAs, the regulatory apparatus is emerging but is still untested. The federal structure of Australian government makes this policy approach more complex and difficult to achieve than in a unitary state like the UK. This is especially so in Australia where no level of government—and neither major political party—has placed housing affordability, specifically, and housing policy, in general, high on the political agenda.

A further regulatory difference, which is perhaps more subtle than the above, arises from differences in the planning systems between the UK and Australia. The UK 1947 Town and Country Planning Act transferred the property rights in development to central government with local planning authorities (LPAs) acting as their agents. When development plans were introduced in the UK in 1990 this fundamental remained unchanged so it was relatively straightforward to introduce affordable housing as a material consideration which enabled LPAs to require developer contributions in the form of land, housing and finance (Crook & Whitehead, 2002; Rydin, 2003).

The evolution of planning in Australia on the other hand meant that, once local plans were in operation, developers were regarded as having regained their property rights in that they had the right to develop if development was consistent with the plan. As a result, in Australia there has to be some form of compensation to developers for giving up their right to maximum profit within the plan. This requires a quid pro quo such as a density premium. The outcome is almost inherently less than can be achieved in the UK although there is no obvious reason why legislation could not be introduced to make the position more favourable for affordable housing.

Nevertheless, because of the relatively narrow ways in which Australian courts have traditionally interpreted planning legislation, the process of driving change through legislative amendment is likely to be more complex than in the British case. For example, in the late 1990s the NSW government amended the Environmental Planning and Assessment Act to allow LAs to require developer contributions for affordable housing. Even so, a large developer successfully appealed the attempt to apply the new rules to its development in inner-Sydney, casting doubt on how effective the amendment would be and at least suggesting that several attempts may be necessary to use the heavy hand of legislation to mandate affordable housing provision (Williams, 2000).

Spiller (2005) has argued persuasively that it may be more feasible for state governments to use new regulatory instruments, based on existing legislation, to impose affordable housing contributions on developers. Most existing legislation requires responsible planning authorities to explicitly measure, conserve and promote social and cultural diversity, opening the door, he argues, to the imposition of inclusionary zoning requiring developers to incorporate affordable housing in their projects or, alternatively, provide cash so that the affordable housing may be provided elsewhere in the neighbourhood.

Governance and political will. The distinction between a unitary system of government, as operates in the UK and a federal system, as operates in Australia, provides a final difference which adds to the problems of transferring the lessons from the UK. This underscores a complicating factor in the use of planning powers in the Australian context, namely, that each state and territory has its own planning system and Act(s). One outcome of the federal system is that prospective developers potentially have to deal with eight different legislative frameworks as well as with a multitude of small local governments. There is currently no clear nationally agreed strategy for harmonising the roles and responsibilities across the three levels of government. There is a potential role for the Commonwealth here in facilitating a common, harmonised approach to land use planning reform (Spiller, 2005).

A final constraint, which is possibly the most problematic of all, arises from a perception among policy makers at all levels that no additional initiatives are needed because of the existence of a substantial private rental market in Australia. Partly as a result of a large number of individual landlords prepared to accept returns well below those required by institutional investors (DSS, 1996; Berry, 2002), this appears to operate relatively effectively and flexibly. The existence of an extensive private rental sector along with the limited subsidies provided through Commonwealth Rent Assistance serves to reduce the pressure on the social rental sector.[10] However, as has been well documented, it falls well short of providing an adequate supply of affordable housing (Yates & Wulff, 2000, 2005).

Opportunities

Despite the qualifications set out above, there are a number of key positive lessons to be learned from an analysis of the factors that have made the UK system work. These relate both to the diversification of the social housing sector through the transfer of LA stock and to its expansion through initiatives to expand the stock of affordable housing.

Transferring the existing stock. First, the Australian States do have significant holdings of public sector housing as well as land and infrastructure associated with this housing stock. Moreover, the current public housing stock in Australia has very little debt associated with it and so does provide some opportunity for the equity in this stock to be used as a means of transferring the stock to new social housing managers (Hall & Berry, 2004). This capacity, however, is constrained by a rent stream that currently is inadequate to cover operating costs.[11] The UK's use of both implicit subsidy, where the calculated sale prices were positive, and explicit subsidy, where the assets had negative values, has been an effective means of sharing the burden between central government and rental incomes. A similar policy in Australia might provide an additional incentive to encourage the States to forego their current ownership of public housing assets.

As, or possibly more, important in the Australian context, has been the way that LSVT and regeneration partnerships have developed mechanisms for realising the value of land and infrastructure assets within social housing areas. The introduction of market housing, commercial property and other higher valued uses in these areas (often under the banner of sustainability and increasing densities) has produced significant potential for cross-subsidy to affordable housing (ODPM, 2005c). This does depend on social ownership of the underlying asserts and the capacity to recycle the revenues obtained from the market sector (HC, 2005).

In order to ensure housing so transferred (or replacements for that housing) remains a part of the affordable housing stock, two key preconditions would need to be met. First, a robust regulatory framework, probably utilising an agency like the Housing Corporation, is necessary. Second, because the success of such an agency is likely to depend upon it, a national consensus in relation to its roles and responsibilities, its structure and its accountability relations is required across the three levels of government that operate in

Australia. Such consensus could be reflected in a new CSHA that established and empowered the agency.

The British experience also offers a clear lesson on how demand-side subsidies (as provided through the HB system) can help to ensure a positive sales value at transfer and therefore generate the capacity to lever in private finance. It highlights the flexibility that follows from demand subsidies being closely related to the real cost of housing faced by households in or at risk of housing stress. In Australia, provision of adequate and secure assistance to the point where rents can be separated from tenant incomes and provision of a secure revenue stream is likely to require a long run, bipartisan commitment to funding adequate subsidy levels for all low income households in need.

Adding to the stock. Adding to the affordable stock with the help of private finance cannot be achieved without subsidy from one source or another, as by definition the tenants cannot pay market rents. The UK experience highlights the fact that there are three main sources of such subsidies: cross-subsidy from the existing stock; cross-subsidy from other stakeholders notably landowners, developers and charities; and direct subsidy from government—and that all have proved necessary to ensure continued new output of affordable housing. The second of these has been the predominant source of subsidy available in Australia over the last decade and then only in very small quantities.

Under the current CSHA a little over $A1 billion is available annually and could be used to provide up-front grants. However, it cannot provide leverage without additional subsidy from other sources because the rental streams will be inadequate to pay an adequate rate of return. On grant structure the UK evidence shows that the certainty of up-front capital grants has made it far easier to introduce private finance into additional mixed funded affordable provision. It also points to its role as a residual funding source (in that HAs bid competitively for SHG), which provides an incentive to maximise other sources of funds.

The two most effective ways of introducing additional subsidy sources in the UK have been the use of the landlord's own equity, and particularly the use of S106 agreements which provide contributions from developers and landowners. In addition employers, particularly quasi-governmental organisations, have on occasion been prepared to contribute land in order to achieve allocations for their employees. In Australia social landlords do not currently have the capacity for internal cross-subsidy. However, the potential for generating resources from more effective overall asset management of the land and infrastructure as well as the housing asset does exist—so with restructuring and a more flexible approach to financing there is considerable potential.

The area where the opportunities, at least in principle, look greatest is in the use of the planning system to help provide both land and a financial contribution to affordable housing. At one level Australia is better placed than the UK in that the market sector is more buoyant so that there is more development where affordable housing might be achieved. So far however although there appears to be a growing willingness to make this type of leverage work, there have been few successful examples (Milligan, 2004). Yet the opportunity clearly exists and relatively small changes in legislation and implementation processes could enable significant leverage of public subsidy.

A new national policy initiative. An historic first joint meeting of the state and federal planning, housing and local government ministers was held in Melbourne in August 2005 in order to address challenges posed by declining housing affordability in Australia.

The meeting agreed to implement a new *Framework for National Action on Affordable Housing* over the 2005–2008 period (JMHLGP, 2005). The first stage of the plan envisages a national review of existing subsidy streams and the development of a national plan for the growth of a viable non-profit housing provider sector. Later stages of the framework will develop reform options, including funding arrangements, for consideration by the ministers in the context of a Coalition of Australian Governments (COAG)-style process.

Although this process has been instigated on a 'collaborative no commitment basis', it indicates a new willingness of Australian policy makers to at least consider the issue of affordable housing within a more holistic policy framework, one that explicitly recognises the cross-government and cross-portfolio connections with broader social and economic policy goals. The institutional machinery established through the *National Framework* exercise may enable Australian policy makers to grasp some of the opportunities discussed above, thereby benefiting from the UK experience.

4. Conclusions

UK policy aimed at levering private finance into the provision of affordable housing was not a carefully defined and well planned and implemented policy aimed at generating a modern approach to the provision of affordable housing in the 21st century. Rather it was a set of incremental measures in response to economic and political imperatives and opportunities (Stephens *et al.*, 2005). The result is a far more flexible housing system but a much smaller, if better organised, social housing sector. Australia, on the other hand, is looking not only to modernise but also to expand the sector.

The introduction of private investment to the social housing sector in the UK stemmed from a government determination to achieve a better social and financial return from the large public investment tied up in the stock. This approach has been used to achieve increased housing standards through upgrading existing publicly owned dwellings, an outcome that would not have occurred in the absence of private investment, given the increasingly tight fiscal constraints on central government and the existing regulatory constraints on local government. Moreover, this privately financed process of consolidation and renewal, alongside the impact of S106 land use planning interventions, opened up the prospect of reducing long-established patterns of urban residential segregation. Nevertheless, these policy gains need to be set next to the fact that social housing in the UK has declined over the period in question. If Australian housing policy makers are to draw on the mechanism of private finance to *grow* as well as modernise the social housing sector, then they will need to satisfy the preconditions summarised below and find the political commitment and adequate public resources to contribute to this goal. This large question lies beyond the scope of this article, which merely seeks to identify the *conditions* for the successful engagement of private finance in social (or more broadly, affordable) housing provision.

The significant role for private finance in the current UK social housing sector points to the advantages of clever institutional design. The regulatory framework constructed over the past two decades and the evolving high levels of confidence and trust generated on all sides has enabled available government subsidy resources to be stretched and a broader range of households assisted.

There is, as noted above, no shortage of proposals to lever private investment into affordable housing provision in Australia (see, e.g. Hall *et al.*, 2001; Wood, 2001; Allen

Consulting Group, 2003). These proposals look to a reinvigorated public borrowing program or fine-tuning of taxation regimes or particular public–private partnerships. However, with only one exception—a one-off deal between the NSW Department of Housing and a large funds manager in the 1980s (Yates, 1994)—the necessary institutional and subsidy arrangements have not been put in place to attract private investment on the scale necessary to make a real positive difference.

A necessary precondition to up-scale private investment—one that was met in the UK in the early 1970s long before rent decontrols in 1988—is to break the nexus between rents received on affordable housing and the incomes of resident households. By allowing social landlords in Australia to charge rents that meet actual operating and financing costs, it is possible to enable them to manage and maintain the stock over the longer term without requiring continued capital or recurrent funding support or forcing declining dwelling standards. However, the link between income and rent cannot be broken equitably without putting in place adequate demand-side subsidies.

Finally, the UK provides a powerful demonstration of the capacity of the land use planning system to capture part of development gain and redirect it into the delivery of affordable housing. As such, policies like S106 deliver on three fronts: they unlock land for HAs and other social housing providers to use, they hypothecate the developer contribution to meeting affordable outcomes and they contribute to broader social policy aims concerning urban regeneration and social inclusion. If Australian governments move in this direction—as NSW and South Australia have shown tentative signs of doing—they will have to find effective ways of amending or replacing existing planning instruments and dealing politically with the predictable opposition of land developers and their allies. One appropriate approach to the need for consistency and reduced negotiation costs would be for the Commonwealth government to broker a national approach to planning law reform in order to 'harmonise' standards across the states and territories, an approach that has been introduced with success in other policy arenas through the Coalition of Australian Governments. A useful start has been made in this direction with the implementation of the *National Framework*.

These preconditions suggest that a concerted effort by the Commonwealth, the States and Local government is required if available resources are to be used effectively to lever in private funding and investment. First the Commonwealth government must make a commitment to an effective regulatory regime which supports the provision of affordable housing; then it must modify and increase current demand-side benefits to ensure greater certainty of revenue streams to the point where asset values are positive and private finance can be levered into the sector. State governments have three major roles. They must first separate rent determination from individual incomes within the social housing system. Secondly, they must restructure their own assets (possibly through transfer or internal reorganisation) to allow existing assets (including land and infrastructure as well as housing) to be recycled in such a way that asset values rise. This will enable private funding to be levered in and asset management skills to be developed. Thirdly, they must put in place land use planning arrangements which make it easier to 'tax' development gains by requiring land and finance for affordable housing. Finally, local governments must work together to produce local plans which both enhance the extent of planning gain by good quality local management and enable this gain to be harnessed to produce additional affordable housing output. Milligan (2005) provides a more detailed analysis of what stakeholders can do to achieve affordable housing goals.

This is not a small agenda. However, a modern housing policy must be based both on using existing assets more effectively and on levering in private resources both through subsidy and funding. The current CSHA points to the way forward but as yet does not support the means for achieving these goals.

Notes

1. *Inter alia*, these covered the need to maintain a core social housing sector and the need to develop and deliver affordable housing options that are non-discriminatory, encourage social and economic participation and provide choice. In addition, they were to specifically target Indigenous people, were to be linked and consistent with broader government objectives, to be cost effective and cooperative between levels of government and, importantly, were "to promote a national, strategic, integrated and long term vision for affordable housing in Australia through a comprehensive approach by all levels of government". A copy of the CSHA can be found at http://www.facs.gov.au/internet/facsinternet.nsf/AboutFaCS/programs/house-csha.htm
2. Much of the detail which supports this article comes from research by the authors undertaken for the Australian Housing and Urban Research Institute on financing affordable housing in Australia and the UK. See Berry *et al.* (2004). The authors wish to thank AHURI for this support.
3. The most relevant instrument that has been operating effectively in the USA is the low income housing tax credit, but this involves tax instruments which are very much more dissimilar (Holmans *et al.*, 2002).
4. For more detail, see Berry *et al.* (2004).
5. For an overview of the housing affordability situation in Australia, see Yates and Gabriel (2006).
6. The SHG is an annual capital grant by central government to HAs for the acquisition of stock.
7. Comparable regulatory arrangements have been established in Scotland, Wales and Northern Ireland.
8. To date, no serious loan defaults have arisen in the social housing sector (HC & NHF, 2005a).
9. It is true that private equity investment has flowed into the private rental market; the so-called 'buy-to-let' market has grown rapidly, with the value of mortgages outstanding increasing by 16 per cent in the second half of 2005 (CML, 2006). However, this outcome has been driven by increasing affordability problems in the low income homeownership market and greater risks in the stock market, than by a concern to provide more affordable housing. Nevertheless, private landlords can access public subsidies through housing homeless people and tenants receiving housing benefit.
10. Commonwealth Rent Assistance is paid to private tenants. This is restricted to social security recipients and is subject to a ceiling which does not reflect the variation in market rents across regions. As a result, it does not cover the gap between what recipients can afford to pay and what it costs to provide their housing, particularly in high cost housing markets. A consideration of initiatives to expand the supply of private rental housing is beyond the scope of this article. Wood (2001) provides examples of what might be done to at least redirect the provision of new private rental stock from the top end of the market to the more affordable stock (see also, Berry, 2002; Allen Consulting Group, 2003).
11. In technical terms, in Australia the net present value of the net income stream is negative which means that the stock has no market value in its current use.

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