

Final Report

A private retail investment vehicle for the community housing sector

authored by

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The authors accept sole responsibility for whatever mistakes remain.

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EXECUTIVE SUMMARY

The Project and its purpose

The purpose of this Project is to attempt to develop a financial product and vehicle through which private retail investors can invest in community housing. It is hoped that such a product will attract new retail investment, but it might also divert current investment in the private rental market to community housing.

Methodology

The Project has unfolded in four stages.

The first stage reviewed the current context, literature and state of play of private investment in social housing. The results are outlined in the Positioning Paper.

The second stage was undertaken in two parts. Firstly, the Project explored the parameters within which community housing organisations (CHOs) operate. Different methods were used to highlight these parameters. The primary methods combined analysis and financial modelling. The results are outlined in the Work-in-Progress Report. Secondly, it involved some indicative 'reality testing' of the housing market in Melbourne and the extent to which recipients of Commonwealth rent assistance (RA) also receive private income. The results of this part are outlined in this Final report.

In the third stage, the Project team prepared a brief to Macquarie Bank (see Appendix I), which responded with a financial product and retail investment vehicle. Macquarie Bank also provided an assessment of this proposal and proposed an alternative approach based on a 'pre-existing and understood market (rather than an untried vehicle)'. The brief and Macquarie Bank's response are discussed in this Final report.

This final stage of the Project draws together the earlier work and findings in order to reflect upon their policy implications for private retail investment in community housing and for social housing more broadly.

Assessing the practicability of private sector investment in community housing

The feasibility of private sector investment in community housing depends upon the cost of acquiring properties and the after-tax income of tenants, which is largely a product of their Centrelink payments and any private income they earn on top of this.

House prices in Melbourne: indicative analysis

The Work-in-Progress Report undertook some modelling which explored the extent to which CHO tenants on Centrelink payments could afford to pay rents high enough to support private investment. On the basis of specified assumptions, the modelling calculated the highest level of house prices that these affordable rents can support. On the one hand, the analysis assumes that these rents are market rents and derives house prices based on these rents. On the other hand, it assumes these rents are sufficient to cover operating costs.

Based on an analysis of house prices in Melbourne, it appears that there would be few if any affordable dwellings available within the major capitals. Those that might be in this range could be expected to be in poor condition and/or on the outskirts of the city.

Private income of Commonwealth RA recipients

The Work-in-Progress Report concluded that the target group for CHOs proposing to utilise private investment are households who, in addition to receiving Centrelink payments (including RA), have other sources of income. So, how many and what proportion of RA recipients are in receipt of private income? What is the level of this private income? What are the characteristics of these recipients? Such an analysis will highlight the groups that a CHO might target in order to utilise private sector investment. It will also pinpoint those that pose higher or lower risks in relation to the CHO's ongoing rental revenue stream.

At December 2000, 66.5% of RA recipients had private income of less than \$50 per week. This has a negligible effect on a CHO's potential rent revenue. The remaining 33.5% had private income of more than \$50 per week. With this level, a CHO's rental revenue will increase by at least \$12.50 per tenant per week. This group of RA recipients has the capacity to increase a CHO's rental revenue such that it can support private sector investment.

The characteristics of those with private income greater than \$50 per week, however, differ from the overall pattern. The largest household type is single persons living alone who make up 38.9% of RA recipients. Indeed, single person households (singles sharing and singles living alone) constitute over 50% of recipients. Yet singles sharing and singles living alone only constitute 25% of RA recipients with private income greater than \$50 per week.

An analysis of the data highlights the following characteristics of RA recipients with private income greater than \$50 per week. The major household types are:

- Sole parents with 1 or 2 children (28.9%); and
- Couples with 1 or 2 children (23.3%).

By Centrelink payment, the major types are:

- Parenting Payment (single) (28.0%); and
- Family Tax Benefit only (27.5%).

By both household type and Centrelink payment, the major types are:

- Sole parents with 1 or 2 children receiving Parenting Payment (single) (23.1%);
- Couples with 1 or 2 children receiving Family Tax Benefit (15.0%);
- Single persons living alone on the Age Pension (8.4%);
- Couples with 3 or more children receiving Family Tax Benefit (6.4%);
- Sole parents with 1 or 2 children receiving Family Tax Benefit, couples with 1 or 2 children receiving Parenting Payment (partnered), and sole parents with 3 or more children receiving Parenting Payment (single) (5.5%, 5.2% and 5.0% respectively); and
- Singles sharing receiving Youth Allowance, and couples receiving the Age Pension (each 4.1%).

While, overall, 33.5% of RA recipients have private income greater than \$50 per week, the incidence is considerably higher within some household types and some types of Centrelink payments:

- Couples with children (69.0%);
- Sole parents with 3 or more children (52.0%);
- Sole parents with 1 or 2 children (48.8%);
- Family Tax Benefit only (100% – by definition);
- Parenting Payment (partnered) (69.1%); and
- Parenting Payment (single) (45.4%).

On the other hand, those receiving Disability Support Pension and Newstart Allowance have a low incidence of private income greater than \$50 per week, at 12.4% and 15.7% respectively.

On the basis of this analysis, the report concludes that a CHO seeking to utilise private sector investment should target the following groups:

- Sole parents with 1 or 2 children receiving Parenting Payment (single);
- Couples with 1 or 2 children or with 3 or more children receiving Family Tax Benefit; and
- Single persons living alone on the Age Pension.

A financial product and investment vehicle for retail investors

Retail investors

Broadly speaking, we can distinguish between two types of retail investors. The first are classic investors who are motivated largely by their expectations of after-tax returns and who make decisions rationally and after considerable research.

The second type are motivated by a broad range of factors, only some of which are financial. Some investors in the private rental market have inherited a property and lease it out while deciding its future. Some prefer to invest in 'bricks and mortar' rather than in financial products, not because the returns are greater but because they believe bricks and mortar to be more reliable and real, while others do so because they can put their own handyman skills to work and thereby build up their own sweat equity while receiving rental income.

The contrast between these two types of investors highlights the major difficulty in developing a financial product and investment vehicle for community housing. As Macquarie Bank explains:

Investors would normally invest in residential property for reasons including potential for capital growth, access to ongoing yield, capital security (real or perceived), availability of tax benefits, ability to actively manage and improve properties, emotional motivations and control over realisation (albeit that liquidity is constrained by property market inefficiencies and high transaction costs). Macquarie's view is that an investment...would need to replicate as closely as possible the characteristics of an investment in residential property in order to maximise its chances of attracting investors.

Attempts to shift a retail investor in private rental to an alternative financial product providing equivalent returns will be difficult. It involves an increasing awareness of the returns on private investment and competition from an array of other financial products.

Brief to Macquarie Bank

The Project team developed a brief to Macquarie Bank which invited them to develop a financial product and investment vehicle drawing on various assumptions concerning prices, rents and dwelling types.

Proposed financial product and investment vehicle

Macquarie Bank proposed a Pooled Fund in which the major participants are:

- Investors who pool their funds;
- CHOs which, on a fee for service basis, manage the properties (both tenancy management and asset management) on behalf of the Pooled Fund and may provide equity funds for joint ventures with the Pooled Fund. In addition, they may provide services such as property acquisition, project development, and oversight of returns to investors;
- Government which provides support to the Pooled Fund through incentives for investors and equity funds for joint ventures with the Pooled Fund or even invests in the Pooled Fund;
- Funds manager who manages the funds raised by the Pooled Fund: this includes investment review and negotiation, funds management, accounting and reporting requirements, promotion, funds and investor administration, and arranging financing for the Pooled Fund and for the investors; and
- Facilitators such as banks, underwriters and insurers which provide funding and support to the Pooled Fund.

Akin to a listed property trust, this type of vehicle would facilitate investor familiarity and optimise tax efficiencies. A single class of securities is proposed, with investors providing funds for each housing project and these funds being allocated at the project level between the various interested parties rather than across the whole Fund. Investment in the Fund would be of an equity nature in order to replicate as closely as possible direct investment in residential property.

Both CHOs and governments could invest directly in community housing projects alongside the Pooled Fund or, alternatively, governments could invest in the Pooled Fund itself.

Finally, Macquarie Bank notes that while there are precedents for this type of vehicle in the investment market in the listed property trust sector (usually commercial and retail property trusts) and infrastructure sector, there are no international precedents in community housing. Given more mature community housing systems and a more sophisticated approach to capital raising in other countries, this suggests that a Pooled Fund may have difficulties successfully operating in Australia.

Assessment of the proposed financial product and investment vehicle

Macquarie Bank considered the investment parameters for the Pooled Fund. Their analysis suggested that 'sophisticated investors in property require a pre-tax return in excess of 10.0% p.a.'. However, based on the assumptions outlined in the brief prepared by the Project team, Macquarie Bank estimated that the pre-tax return and pre-tax internal rate of return (which includes capital growth) on the Pooled Fund for community housing are in order of 3.0% p.a. (and growing at the rate of inflation) and approximately 6.0% p.a. respectively. On this basis, the Pooled Fund would require significant subsidies if commercial rates of return are to be achieved.

They conclude:

Macquarie considers that the risks, costs and rigidity of a Pooled Fund are likely to outweigh any benefit that it may provide as a source of significant funds for community housing.

An alternative proposal for private investment in community housing

Macquarie Bank also considered an alternative approach to the pooled fund, which builds upon the strengths of private rental investment as a 'cottage industry'. This alternative approach is to provide financial incentives for investors in the private rental market to lease dwellings to CHOs. Macquarie's particular proposal is a tax exemption on a proportion of rental income (for example, 20%) where the owner leases a dwelling to a CHO for a minimum period of, say, five years. The level of this incentive could be varied over time in order to ensure a regular supply of stock at minimum cost to government.

Macquarie believes that this will not only provide incentives for investors in the current cottage industry but also has the potential to encourage new investment in cluster and larger-scale developments.

Policy implications

Policy implications for community housing

The research has, unfortunately, provided little optimism for the future. The literature, the experience in other countries and advice from the finance industry all indicate that private sector investment in community housing is highly unlikely without higher levels of government support and subsidy than is currently the case.

No private investment in community housing without government intervention

If CHOs are to utilise private retail investment for the expansion of community housing, then some form of additional government intervention is necessary. This could take the form of capital subsidies (in the form of free equity) or operating subsidies directly to CHOs (in addition to RA). At the Commonwealth level, there could be changes in capital gains and income tax provisions or taxation concessions. At the state level, there could be land tax exemptions, stamp duty exemptions, council and water rate concessions etc. No one arrangement is probably sufficient to enable a CHO to break even.

Capital funds from government are necessary

The research has highlighted the extent to which many of those dependent on a Centrelink payment are only able to afford rents that cover the operating costs of providing community housing. Indeed, the income of some groups such as young people are inadequate to meet even operating costs. Without a continuing stream of capital subsidies or free equity, or without a substantial boost to benefit levels, these households will continue to be vulnerable to extreme housing stress.

The target group for CHOs utilising private sector investment

Private sector investment in community housing will only be financially feasible for CHOs targeting low income households that receive some private income in addition to their Centrelink payments.

Cost-effective private sector investment

The most cost-effective schemes for attracting private sector investment are likely to be those which most closely approximate the existing private rental market where expectations of returns are low by comparison to more sophisticated vehicles with a similar risk profile.

Key role for CHOs

The best way to attract private investment into a form of housing which guarantees outcomes for tenants is through a financial incentive which is linked to an accredited CHO. This is a key component of Macquarie Bank's alternative approach.

The form of the financial incentive

The most simple and manageable form of financial incentive is likely to be a tax exemption on a proportion of the income derived from investment. Further work still needs to be done on the level of this incentive and how the adjustments might occur.

Community housing tenants continue to remain eligible for RA

CHOs can utilise some retail investment for community housing. However, this is highly dependent upon maximising the extent to which they can capture RA. They can only do this if community housing tenants continue to be eligible.

Alternative rent setting policies

In order for CHOs to manage schemes involving private sector investment, including Macquarie Bank's alternative approach, it will be necessary to adopt alternative rent setting policies which provide greater predictability in their rental income. Such policies are only necessary where the CHO is utilising private sector investment and thus where tenants are in receipt of relatively high incomes.

Risk management and CHOs

If the community sector is to utilise private sector investment, it is imperative that CHOs implement strategies to enhance their risk management capacities. Initially, they will need to build up considerable expertise in the private rental sector as well as housing finance and housing economics.

A regulatory regime which provides specific accreditation to CHOs utilising private sector investment is necessary to provide assurance to private investors and public accountability. Future autonomy promised by private investment in CHOs must be weighed against their capacity and skill to manage risks.

Policy implications for the housing market

Reform of the private rental market

A critical issue for reform of the sector and its long-term future is to encourage corporate and institutional landlords into the market. This is most unlikely without significant increases in market rents, and subsequent demands for increases in government support for low and middle income tenants. Among the alternatives facing government are:

- Do nothing and so maintain the status quo – the cottage industry – and live with an industry that generally does not meet the needs of tenants and deliver quality services;
- Introduce some reform of the private rental sector – a better focus on tenant outcomes and delivery of quality services – by supporting alternative approaches which combine the strengths of both the private and community sectors; and
- Fund and support an alternative housing sector such as the social housing sector where leakage of funds into other activities is very limited.

Macquarie Bank's approach is within the second alternative. It brings together private equity investors and CHOs focused on tenant outcomes and the delivery of quality services.

Private investment in social housing

Free equity is particularly important if social housing providers are to target those households whose sole source of income is a Centrelink payment.

However, the analysis in this Project has differentiated between those households who rely solely upon Centrelink payments and those who supplement these with other sources of income. It is households within this latter group who have, to varying levels, a capacity to support private sector investment in social housing.

Despite a long history of attempts to utilise private sector investment in community housing, neither the Commonwealth nor the state governments have reached agreement on an appropriate vehicle. It is now critical that they develop a national vehicle which will attract private sector funds and which is available to all social housing providers.

GLOSSARY OF TERMS

Affordable rent: Rent determined to be affordable to tenants. It is based upon the Victorian Office of Housing rent formula plus any entitlement to RA. It is the rent charged by a CHO (see Appendix II for more details).

Bond: A debt investment where funds are lent to an entity (company or government) for a defined period of time at a specified interest rate. In exchange for these funds, the entity issues a certificate, or bond, that states the interest rate to be paid and when funds are to be returned, or the maturity date of the bond. Interest on bonds is usually paid every six months (semi-annually).

Capital-indexed loan: A loan where the interest rate applied to the principal is set in real terms and adjusted for inflation. The outstanding principal is also increased annually by the rate of inflation.

Credit foncier loan: A common type of housing loan where debt and interest are repaid in equal instalments over the term of the loan (provided that the interest is not varied).

Debt financing: When a firm raises money for working capital or for capital expenditure by selling bonds, bills or notes to individual or institutional investors. In return for lending the money, the individuals or institutions become creditors and receive a promise to repay principal and interest on the debt.

Equities and units in trusts: Shares traded on an organised stock exchange, shares in unlisted companies, convertible notes after conversion, preference shares and units issued by both listed and unlisted unit trusts. Trust units are included in this classification because they have important characteristics of equities, such as entitlement to a share of the profits and (on liquidation) of the residual assets of the trust.

Equity finance: A type of capital finance where funds are raised from a private sector investor by issuing of equity shares in an underlying asset. Returns to the investor, such as income return (dividend) and capital growth, are based on the performance of the underlying assets and are therefore uncertain.

Equity: This term has two meanings. The first is often the basis of public policy and is concerned with the relative costs of housing between households: households in similar circumstances should pay similar costs, and households with higher incomes should pay higher costs. The second relates to a stake in an investment and involves residual claims on income, with the returns taking the form of dividends or capital gains.

Ethical investors: Seek to secure market rates of return on investments. They avoid investments which they regard as detrimental to the environment and to society or choose investments which they regard as environmentally or socially beneficial.

Financial asset: An asset which has a counterpart liability in the books of another accounting entity.

Free equity: Funds for capital purposes which are provided by government, church or other organisations either indefinitely or for very long periods without financial returns. These can be in the form of land or loans secured through mortgage, debenture or agreement. Examples include CSHA grant funds and land provided by churches for joint ventures.

Gearing: The extent to which an entity's assets have been acquired using debt. The gearing ratio is the proportion of assets funded through debt. It is usually expressed as a percentage of assets.

GST-free supply: A supply of goods and services where no GST is charged and the supplier can claim input tax credits for GST paid on purchases or expenses in relation to that supply.

Headlease: A lease between an owner of a property and an agency which intends to sub-let to an individual tenant.

Housing bonds: Different types of securities which are issued to raise funds for housing purposes. These funds are on-lent to owner-occupiers and social housing providers.

Input tax credit: The GST which a business has paid on its inputs (purchases/expenses) and can claim back from the Australian Taxation Office. The credit is offset against any GST collected from the sale of taxable supplies.

- Input-taxed supply:** A supply of goods and/or services where GST is not charged and the supplier cannot claim input tax credits on purchases or expenses related to that supply, e.g. the provision of residential accommodation in the private sector.
- Institutional investors:** Organisations which have large sums of money to invest. They specialise in raising funds from the public and investing these funds. For example, superannuation funds, life funds, insurance companies, banks and unit trusts.
- Interest-only loan:** A loan that requires only interest payments over its agreed term with no repayment of capital until the end of the loan. At the end of the term, the loan capital is required to be repaid in full, or the loan renegotiated for another fixed term.
- Land and buildings:** Real estate or physical assets which are immovable.
- Loan:** The transfer of an asset (usually money) from its owner (the lender) to a user (the borrower) in return for a fee (usually interest).
- Market rent:** Rent agreed between a private landlord and a tenant within a market economy.
- Market-derived rent:** The term used throughout this report to indicate that the so-called market rent for social housing dwellings is derived through an administrative process which seeks to establish the rent which a particular property would receive in the private rental market. This rent is derived administratively, rather than through a process which actually tests the rent within the market place.
- Mortgage:** A document which conveys or assigns an interest in an asset (such as a dwelling) to a lender (such as bank) as security against a loan. The borrower is obligated to make a predetermined set of payments to repay the loan. The borrower has use of the asset and can discharge the mortgage upon fulfilment of the mortgage contract. In the case of default (on repayments), the asset is sold and the lender has first call on the proceeds of the sale.
- Rate of return:** The ratio of income to capital investment, usually expressed as a percentage.
- Real interest rate:** The difference between nominal interest and an amount equal to the loss of purchasing power on the monetary value of the principal during the accounting period. It is calculated by subtracting the rate of inflation from the nominal interest rate.
- Real-rate finance:** Loans or securities which are adjusted for inflation. The capital component increases by the rate of inflation while interest payments are based on the real rate of interest.
- Real-rate securities:** Securities where the coupon rate is the real interest rate. The capital component increases by the rate of inflation while interest payments are based on the real interest rate.
- Retail investors:** Individuals or small organisations seeking market rates of return on their investments.
- Securities:** Bills, bonds, certificates of deposit, commercial paper, debentures, financial derivatives, and similar instruments normally traded in the financial markets.
- Social investors:** Accept below market rates of return while investing in projects which provide for the common good or achieve a particular social outcome.
- Steady-state financial position:** The term used throughout this report to describe the financial objective of a CHO. Its meaning is discussed more fully in Appendix I.
- Unit trust:** An organisation that collects cash investments from subscribers, the unit holders, and invests in securities for their benefit. Each unit holder is an owner of a fraction of the securities held by the trust.
- Yield:** The income from an investment such as real property, bonds, shares and units as a proportion of its current market value or price.

This glossary has been compiled largely from those in the following publications:

- ABS (2000) *Finance Australia 1999-2000*, Cat. no. 5611.0, Australian Bureau of Statistics, Canberra;
- Caversham Partners Ltd et al. (1991) *Report on Alternative Ways of Raising Private Sector Finance for Social Rental Housing*, Department of Health, Housing and Community Services, Canberra;
- Penguin Macquarie (1988) *The Penguin Macquarie Dictionary of Economics and Finance*, Penguin, Melbourne.

1. INTRODUCTION

For over fifty-five years, there have been two cornerstones of social housing provision in Australia: public housing, and the Commonwealth-State Housing Agreement, with the latter being the funding mechanism for the former. More recently, the community housing sector has been growing more rapidly from its small base, and the Commonwealth government has been encouraging private investment in social housing as a supplement to public investment.

For some time now, the community housing sector has effectively drawn on retail investment by headleasing dwellings from the private sector. Under these arrangements, the private retail investor receives the rate of return currently prevailing in the private rental market and invests on this basis. Financial rather than social concerns are dominant. Over the past two decades, State Housing Authorities have appreciated the limitations of headleasing and have investigated other ways of encouraging private sector investment in housing, particularly institutional investors. Very little work has been done, however, to encourage small-scale retail investment in social housing, even though this category of investors is the mainstay of the private rental sector in the form of small-scale investors owning one or two dwellings.¹

1.1 The Project and its purpose

The purpose of this research Project is to attempt to develop a financial product and vehicle through which private retail investors can invest in community housing. A financial product and investment vehicle of this type should be attractive to retail investors without increasing the costs to CHOs beyond what they can already pay for headleased properties. It is hoped that such a financial product and investment vehicle will attract new retail investment, but it might also divert current investment in the private rental market to community housing.

The key question is: Can retail investment in housing be channelled into community housing at or below the currently prevailing rate of return provided by the private rental market, and if so, how?

This requires an understanding of both the parameters within which community housing managers operate and the characteristics of and parameters for retail investors (as distinct from institutional investors). There are a number of related issues that need to be addressed. These include:

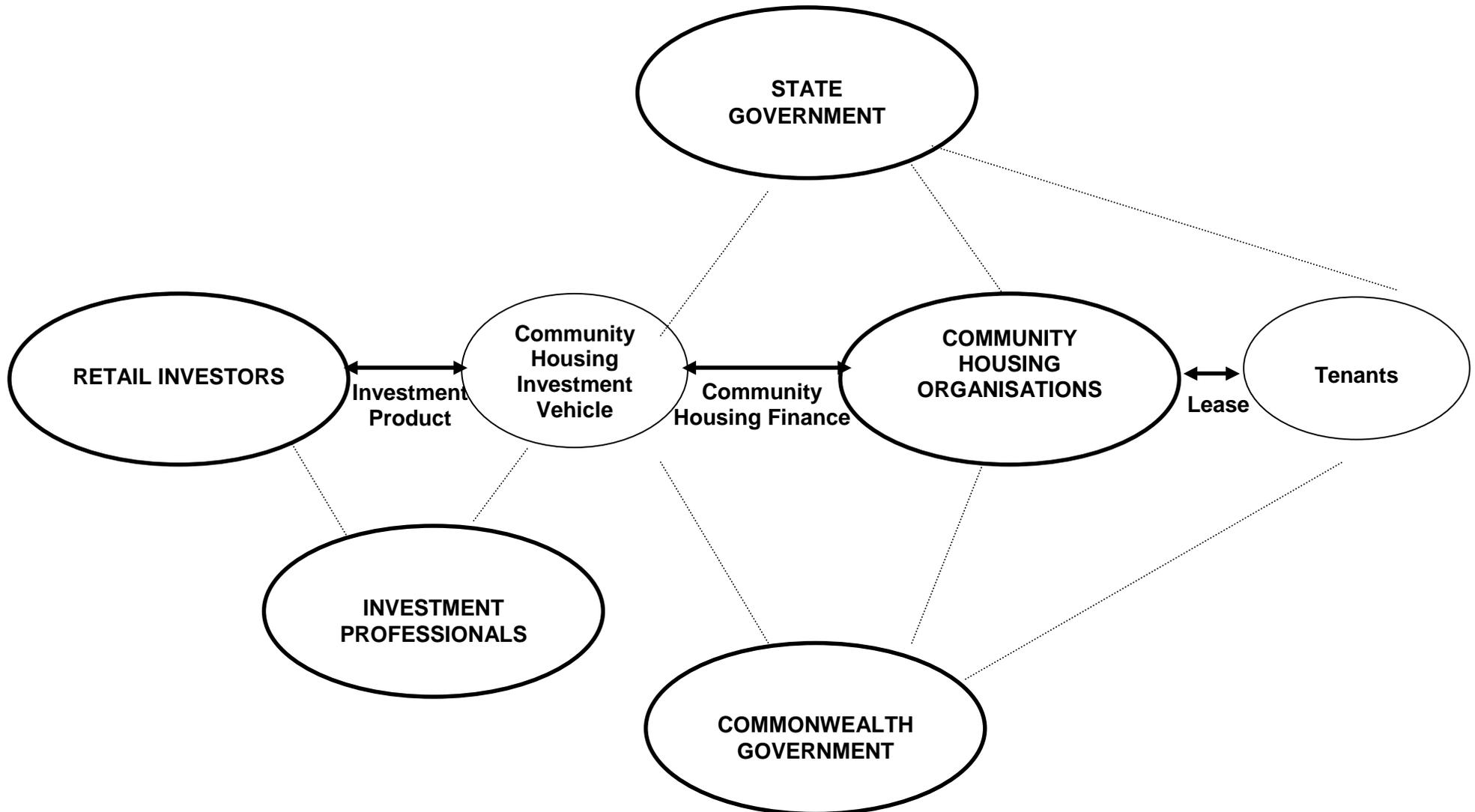
- The barriers to retail investors investing in low income housing and what might be done to overcome them;
- The potential of the private retail investment market and its investment requirements;
- The policy levers available to Commonwealth and state governments which might be used to increase the level of retail private investment in community housing; and
- The fiscal, administrative and economic implications of the models developed to raise retail private investment in community housing.

1.2 Conceptual framework for the Project

Diagram 1 illustrates the relationships that form the focus of this Project. The two major parties involved are **CHOs** and **retail investors**. The relationship between them is mediated by **investment professionals** who develop financial products and vehicles which bring the parties together. **Commonwealth and state governments** play a specific role in support of private sector investment in community housing. Jointly, both levels of government determine the regulatory framework for CHOs, retail investors and investment professionals.

¹ For details, see the Positioning Paper <www.ahuri.edu.au/pubs/positioning/pp_privateinvestment.pdf>, pp. 1-4.

Diagram 1: Conceptual framework for developing an appropriate product and mechanism for private sector investment in community housing



Both CHOs and retail investors have their requirements and parameters for participating in a financial product and associated investment vehicle. An appropriate financial product and vehicle for investment in community housing is one which meets or largely meets the requirements and parameters of both parties. These two groups have very different motivations, and imply very different policy interventions. The Project therefore explores their expectations, their respective risks and their preferences in relation to financial and investment products.

The Commonwealth government determines the framework within which a financial product and vehicle will be developed. It determines the taxation provisions and concessions in relation to income tax and capital gains tax which will or may apply. It determines the level, scope and structure of RA and other subsidies that may directly relate to social housing investment. It may provide capital funds to support the acquisition of community housing.

State governments provide the regulatory framework and support the infrastructure for community housing. Through this regulatory framework, they monitor the standards of service provided by CHOs. State governments determine the extent to which CHOs are subject to land tax and any financial product is subject to stamp duty and other taxes. They can also provide operational subsidies and/or capital funds.

1.3 Methodology

The Project has unfolded in four stages, with each stage adopting a specific methodology.

The **first** stage reviewed the current context, current literature and current state of play of private investment in social housing. The methodology involved a review of the relevant literature in order to scope the issue more fully and to describe and analyse the various ways in which CHOs have financed the acquisition of housing. The results are outlined in a Positioning Paper <www.ahuri.edu.au/pubs/positioning/pp_privateinvestment.pdf>, which is summarised in Section 2.1 below.

In the **second** stage, the Project explored the parameters within which CHOs operate. Different methods were used to highlight these parameters. The primary methods combined analysis and financial modelling that analysed:

- Housing as an investment and a commodity;
- Community housing's objectives, underlying philosophy and target group;
- Community housing finances;
- The impact of different assumptions on the financial viability of CHOs; and
- The implication of the financial modelling for (i) capital and operating subsidies, (ii) community housing infrastructure and management, and (iii) Commonwealth and state governments.

The Work-in-Progress Report <www.ahuri.edu.au/pubs/progress/pr_privateinvestment.pdf> outlines this stage and reports on its preliminary findings, which are summarised in Section 2.2 below.

The second stage also included a workshop on the Work-in-Progress Report and some indicative 'reality testing' on the extent to which RA recipients receive private income and can support private sector investment. It also provided an analysis of the Melbourne property market to find out what proportion of properties are sold within particular ranges. The results are outlined in Section 3 below.

In the **third** stage, the Project team prepared a brief to Macquarie Bank (see Appendix I), which responded with a financial product and investment vehicle through which retail investors could invest in community housing. They also provided an assessment of this proposal and proposed an alternative approach based on a 'pre-existing and understood market (rather than an untried vehicle)'. Macquarie Bank undertook this work on a *pro bono* basis. The results are outlined in Section 4 below.

The **final** stage of the Project drew together the work and findings of the preceding stages in order to reflect upon the implications for private retail investment in community housing and for social housing more broadly. Section 5 highlights the difficulties faced by retail investors and CHOs, the potential for private retail investment, the role which Commonwealth and state governments need to play, and the fiscal, administrative and economic implications.

2. SUMMARY OF PREVIOUS WORK

2.1 Positioning Paper: summary

The Positioning Paper <www.ahuri.edu.au//pubs/positioning/pp_privateinvestment.pdf> sets the scene by examining the context in which the Project has come to the fore as a policy issue and the current state of play in regard to private sector investment in social housing.

The review of the policy context notes:

- Continuing market failure within the private rental sector and the attendant need for a vibrant and viable social housing sector;
- The decline in CSHA funding, resulting in a very slow increase in social housing stock in the face of substantial unmet need;
- Substantial increases in RA over the past decade, reflecting the Commonwealth's confidence in the private rental sector as a provider of adequate and affordable housing for low income households, as well as a preference for RA as the main form of housing assistance;
- The slow expansion of community housing, and the considerable time and energy being invested in national and state infrastructure to support its ongoing development, in part to attract private sector investment; and
- The three classes of investors (institutional, retail and social) and the size and scope of their investments.

The second part of the Positioning Paper explored the limited literature on private sector investment in social housing and a range of models of social housing finance which are currently operating. It concluded that:

- The current literature on financing social housing through private sector investment has focused predominantly on institutional investors rather than retail investors. Further work on the characteristics and expectations of retail investors may open up the potential of this group to invest in community housing;
- Since the early 1980s, extensive work has been undertaken on different forms of debt finance – in particular, housing bonds – as a source of funds for social housing. These provide a starting point for considering financial products and investment vehicles appropriate for retail investment in community housing;
- Private investment has particular implications for the financial viability and management of CHOs. It will not only mean higher ongoing costs but will require management to give greater emphasis to prudential standards, financial controls, risk management and formal accountability; and
- Taxation arrangements are critical to the success of financial products through which private sector investment can be raised for social housing. More broadly, the Project will need to take into account the different contexts for financial products, the impacts of current taxation arrangements, and the possible role of both Commonwealth and state governments supporting the products in various ways.

2.2 Work-in-Progress Report: summary

Stage 2 of the Project sought to establish the parameters within which CHOs might sustain private investment in community housing. In general terms, the primary parameters for a CHO stem from their social housing objectives. Secondary parameters are determined by their financial objectives and largely relate to their capacity to sustain private sector investment, given their revenue flows from low income tenants.

Thus, Stage 2 involved an analysis of housing as an investment and a commodity. Along the way, it also examined the objectives and characteristics of community housing as well as its primary target group, and then explored the implications for community housing finance.

The Work-in-Progress Report <www.ahuri.edu.au/pubs/progress/pr_privateinvestment.pdf> began with an exploration of the relationships between the level of capital investment, the impact of different sources and types of capital investment, operating costs, revenue from tenants, and the availability and limitations of subsidies. A CHO can only borrow capital funds when they can service loans. Repayments will vary according to the type of loan, the interest rate, how often repayments are made, and over what period the loan is to be repaid. Their capacity to repay these loans will depend upon their rental revenue and their other costs. If revenue is lower than operating costs, they will have no capacity to repay loans. If revenue is greater than operating costs, then they have a capacity to do this.

The second phase of Stage 2 analysed the primary target group of community housing – those eligible to receive Commonwealth RA. The key issue for CHOs is the level of rental revenue they can expect to receive, assuming a particular rental benchmark (determined to be 25% of income plus entitlement to RA). A range of scenarios were examined to identify the range of rents which a CHO could receive for each dwelling size according to household type.

The third phase of Stage 2 explored the financial parameters for CHOs and their capacity to support private investment by modelling a CHO's revenue and operating costs while making a series of assumptions about the housing market and operating costs. In particular, it explored the capacity of a CHO to support headleasing, and debt finance, where the rents charged are equivalent to market rents. Affordable house price ranges were also explored.

The fourth phase developed a typology of housing subsidies based upon the foregoing analysis and the extent to which a CHO requires support for capital funding.

The final phase of this stage is outlined in this final report. Of interest is the feasibility of securing private sector finance for community housing, given certain assumptions about variations in house prices and the extent to which a CHO can borrow funds, a capability in turn dependent on tenants' incomes.

The preliminary findings of the first four phases are summarised below under five headings: social objectives; characteristics of the community housing sector; financial parameters; implications for a financial product and investment vehicle; and gaps in our knowledge.

(1) Social objectives

The primary operating parameters for a CHO are the social objectives which they seek to achieve. These include:

- A particular target group;
- An affordability benchmark; and
- A commitment to acceptable levels of quality, amenity and appropriateness of the housing stock.

The way in which each of these is defined will affect the financial parameters and the extent to which a CHO can utilise private investment.

As CHOs seek to extend the level of private sector investment, the definition and the way in which each of these social objectives is measured may come under increasing pressure. For instance, a CHO can extend the level of private investment or reduce its risks by:

- Working towards an affordability benchmark of 30% income rather than 25% income;
- Providing limited tenure rather than security of tenure;
- Reducing the level of service to tenants;
- Reducing the level of amenity provided to tenants; and
- Acquiring dwellings in locations which provide greater levels of return to investors, rather than in locations which meet the needs of tenants.

As CHOs confront the risks inherent in private investment, they will have to make difficult decisions about the degree to which they wish to spread the benefits they provide to a wider number of tenants, albeit at reduced rates.

(2) Characteristics of the community housing sector

The community housing sector as a whole has characteristics which also affect its capacity and willingness to draw upon private investment. These include:

- The dominance of small-scale organisations operating within local areas, rather than a few larger ones operating across regions, preventing them from benefiting from economies of scale;
- The dispersal of the asset base across a relatively large number of organisations; and
- A desire for rapid expansion.

As a result, local variables impact considerably upon the operations of CHOs. The analysis of community housing finances presented in the Work-in-Progress Report is based on broad assumptions about how the housing market operates.

(3) Financial parameters

There are important inter-relationships between capital finance (and house prices), rental revenue (and Centrelink payments including RA), ongoing costs and subsidies. These need to be better understood if CHOs are to properly assess their capacity to use private investment for capital purposes. The financial parameters cannot be described in fixed terms, because of:

- Variations in house prices and rents, which differ within and between states, and which will affect and be affected by CHOs' decisions about standards of amenity;
- The type, form and cost of capital finance, which will tend to move in line with the business cycle;
- The income profile of tenants, which depends upon decisions of the CHO and upon the level and structure of Centrelink payments; and
- The subsidies and other supports which CHOs can receive from Commonwealth, state and local governments.

Financial modelling highlights the importance of government equity funding even where tenants can afford market-derived rents. Rent revenue even from market-derived rents is inadequate to meet both operating costs and the financial costs of providing community housing. Thus some level of free equity is required if CHOs are to be financially viable.

Private investment in community housing will increase the policy, financial and management risks for CHOs. Different forms and types of capital finance have different implications for maintaining a steady-state financial performance, for their consideration of risk-averse capital finance strategies, for their long-term financial viability, for their control over properties, and for their capacity to meet social objectives such as affordability, appropriate housing and security of tenure. To date, the preferred capital finance option of CHOs is free equity, which is relatively risk-free.

RA is important in improving the capacity of CHOs to use private investment for capital purposes. On the other hand, they will have to consider the consistency of the policy framework over a very long term. Of particular importance is the extent to which any changes to the levels and structure of RA will impact on their rental revenue.

The taxation conditions under which CHOs operate may offset operating and acquisition costs, allowing the financial parameters to be loosened. While significant, taxation conditions are secondary to other measures in maintaining their financial viability.

Where a CHO is proposing to utilise private investment in community housing, their target group for tenancy will become:

- Households who in addition to receiving Centrelink payments have other sources of income such that they pay higher levels of affordable rents – the higher their additional income, the higher the level of retail investment that can be utilised; and
- Households paying market rents.

Rent revenue for CHOs is largely related to the levels of Centrelink payments, because the majority of community housing tenants rely upon such income support. The level and structure of these payments determines the affordable rents paid by tenants. On the other hand, the extent to which a CHO can utilise private sector investment is constrained by rental revenue, which is in turn determined largely by Centrelink rules, regulations and payment rates. It can only utilise private sector investment where the income profile of tenants allows for a surplus after operating costs and a provision for depreciation are met.

The Work-in-Progress Report draws attention to the inadequacy of some Centrelink payments, particularly those received by young people. Even if an affordable rent is charged, rent revenue for a CHO is likely to be insufficient to meet basic operating costs.

(4) Implications for a financial product and investment vehicle

A financial product and investment vehicle for channelling private retail investment into community housing should:

- Provide rates and conditions which are better than can be achieved through current mortgage rates. Alternatively, it will provide equivalent rates and conditions but provide debt or equity finance on a basis which better matches the revenue flows of the CHO;
- Be flexible enough to allow the CHO to mix free equity with private sector investment;
- Address the risks which the CHO has in utilising private sector investment, viz. where there is a change in household circumstances or a mismatch between revenue and the costs of finance; and
- Offer a variety of both debt and equity finance instruments.

(5) Gaps in our knowledge

The financial modelling undertaken for this Project highlights some major gaps in our knowledge:

- There are no generally accepted evidence-based benchmarks for operating costs;
- The provision for depreciation is conceptually unclear, shifting between an accounting notion, a notion related to building refurbishment, and a notion related to obsolescence of technology and bringing a dwelling up to contemporary standards;
- As a result of the conceptual difficulties, the basis on which the provision for depreciation is calculated is unexplored; and
- Little work has been undertaken on whether and to what extent market rent as a rate of return varies between states, regions and market segments. The exception is the work of Yates and Wood (1997).

3. ASSESSING THE PRACTICABILITY OF PRIVATE SECTOR INVESTMENT IN COMMUNITY HOUSING

The feasibility of private sector investment in community housing depends upon the private income of tenants (in addition to Centrelink payments) and house prices. This section undertakes some indicative 'reality testing' by examining house prices in Melbourne and by analysing the extent of private income among RA recipients.

3.1 House prices in Melbourne: indicative analysis

The range of rents payable by CHO tenants receiving Centrelink payments is determined largely by the level of these payments. The Work-in-Progress Report undertook some modelling which demonstrated the extent to which this affected potential rent levels. Some of this is reproduced in Table 1.² Column A outlines the highest affordable rents³ for each size of dwelling occupied by families whose only source of income is a Centrelink payment.

Table 1: House prices supported by rents charged to tenants whose only source of income is a Centrelink payment (families only), June 2001

	A	B	C
	Highest affordable weekly rent	House price (assuming rent is a market rent)	House price (assuming rent is used to meet operating costs only)
2 bedroom dwelling	\$104	\$83,227	\$173,252
3 bedroom dwelling	\$166	\$133,323	\$277,535
4 bedroom dwelling	\$173	\$138,753	\$288,837

If this affordable rent is regarded as a market rent, then Column B outlines the maximum house prices that can be supported with these rents.⁴ The market rent is the highest rent which a CHO can charge. Where houses are acquired at these prices, the CHO can support the maximum level of private investment. As it acquires dwellings above these prices, more rent is directed to operating costs and less to finance costs (and supporting private investment).

Column C shows the maximum house prices that could be afforded by a CHO renting dwellings to families on RA, assuming that all of the affordable rental payments are used to cover all operating costs and depreciation.⁵ If a CHO acquires dwellings above these prices, they will require additional operating subsidies to meet operating costs and depreciation.

There would be few if any appropriate dwellings available within the major capitals that could be purchased within the prices outlined in Column B. Those that might be in this range could be expected to be in poor condition and/or on the outskirts of the city.

As an example, consider Table , which shows the proportion of properties in Melbourne that were sold in 1999 at or below \$150,000, at a time when prices were up to 50% lower than they are today. The figures are broken down by region. Less than 8% of all dwellings sold for less than \$100,000, and almost all of these were in the outer suburbs. Today, it is likely that no properties in Melbourne would sell for less than \$100,000.

² This table is derived from Work-in-Progress Report, Table 6, p. 24.

³ For a description of how this 'affordable rent' is calculated, see Work-in-Progress Report, Appendix II, p. 36. Broadly, it is based on the Victorian Office of Housing rent formula plus entitlement to RA. This rent formula is 25% of the gross assessable income for adults in the household plus 11% of any Family Tax Benefit.

⁴ See Work-in-Progress Report, p. 24, where this analysis is discussed in more detail and annual market rent is assumed to be 6.5% of house value.

⁵ See Work-in-Progress Report, p. 24, where this analysis is discussed in more detail and it is assumed that annual operating costs are 1.92% property value and annual depreciation is 1.2% of property value.

Even if properties were available at these values, the maximum debt finance a CHO could support is 40% of these house prices. This begs the question of where the remaining capital is to be found.

Table 2: Percentage of properties sold in Melbourne in 1999 at or below various prices

Range	Percentage							
	Total Inner	Outer West	North West	North East	Outer East	South East	Morn. Penin'a	Greater Melb
\$60,000	0.3	1.5	0.8	0.5	1.2	1.4	2.5	1.0
\$80,000	0.4	3.8	2.5	0.7	3.1	4.5	8.5	2.8
\$100,000	0.9	10.9	7.0	2.7	7.0	16.7	16.4	7.3
\$150,000	7.9	36.5	38.0	28.1	44.7	52.5	37.8	29.4

Source: Valuer General unit sales records for 1999

3.2 Private income of RA recipients

The capacity of CHOs to support private sector investment depends upon the private income of RA recipients. The analysis of revenue based on affordable rents in the Work-in-Progress Report demonstrates that, where tenants are reliant solely upon Centrelink payments, CHOs are only able to support minimal – if any – private sector investment. Only where tenants have additional private income will the CHO receive sufficient rental income to cover not only their operating costs and depreciation but also the costs associated with attracting private sector investment:

Where a CHO is proposing to utilise private investment in community housing, its target group for tenancy will become:

- *Households who, in addition to receiving Centrelink payments, have other sources of income such that they pay higher levels of affordable rents (the higher their additional income, the higher the level of retail investment that can be utilised); and*
- *Households paying market rents (Work-in-Progress Report, p. 29).*

So how many and what proportion of RA recipients are in receipt of private income? What is the level of this private income? What are the characteristics of the recipients? The analysis of the data in this section proceeds through four stages:

- An overview of the extent of private income among RA recipients;
- Household types receiving RA and those with private income greater than \$50 per week;
- Types of Centrelink payments received by RA recipients and those with private income greater than \$50 per week; and
- Household types and types of Centrelink payments received by RA recipients and those with private income greater than \$50 per week.

This analysis seeks to identify:

- The characteristics of the largest groups of RA recipients (household types and types of Centrelink payments) with private income greater than \$50 per week; and
- The characteristics of those groups with the highest incidence of RA recipients with private income greater than \$50 per week.

This analysis will highlight the groups that a CHO might target in order to utilise private sector investment. It will also pinpoint those that pose higher or lower risks in relation to its ongoing rental revenue stream.

(1) *Overview of RA recipients*

Table shows the private income received by RA recipients, divided into two groups: those receiving a pension or allowance (such as Age Pension, Parenting Payment, Youth Allowance, Newstart and Disability Pension); and those receiving Family Tax Benefit only (i.e. families where adults are working).

66.5% of RA recipients have private income of less than \$50 per week. This has a negligible effect on a CHO's potential rent revenue. The remaining 33.5% have private income of more than \$50 per week. With this level, rental revenue will increase by at least \$12.50 per tenant per week. This group of RA recipients has the capacity to increase a CHO's rental revenue such that it can support private sector investment.

Table 3: RA recipients by private income, December 2000

Level of private income	#	%
Pensions and allowances		
<\$50 per week	591,038	66.5
\$50-\$100 per week	64,249	7.2
\$100+ per week	151,328	17.0
Family Tax Benefit only		
<\$550 per week	29,592	3.3
\$550-\$750 per week	33,813	3.8
\$750-\$1,000 per week	16,672	1.9
\$1,000+ per week	1,694	0.2
Total	888,386	100.0

Source: Data provided by the Commonwealth Department of Family and Community Services

(2) *RA recipients by household type*

Table 4: Number and percentage by household type, all RA recipients and recipients with private income >\$50 per week, December 2000

Household type	All recipients		Recipients with private income >\$50 per week	
	#	%	#	%
Singles sharing	128,111	14.4	22,709	7.6
Single person (independent)	345,604	38.9	50,524	17.0
Couple	65,432	7.4	23,516	7.9
Sole parent with 1 or 2 children	176,016	19.8	85,872	28.9
Sole parent with 3+ children	31,651	3.6	16,460	5.5
Couple with 1 or 2 children	99,921	11.2	69,392	23.3
Couple with 3+ children	41,651	4.7	28,875	9.7
Total	888,386	100.0	297,348	100.0

Source: Data provided by the Commonwealth Department of Family and Community Services

Table 4 shows that the largest household type is single persons living alone who make up 38.9% of RA recipients. Indeed, single person households (sharing or living alone) constitute over 50% of RA recipients. It also includes a breakdown by household type of those receiving more than \$50 per week in private income.

The major household types receiving more than \$50 per week in private income are:

- Sole parents with 1 or 2 children (85,872 households or 28.9%); and
- Couples with 1 or 2 children (69,392 or 23.3%).

Single persons (both sharing and independent) constitute nearly 25% of RA recipients with private income greater than \$50 per week.

The incidence of household types receiving RA with private income greater than \$50 per week is outlined in Table below. While, overall, 33.5% of RA recipients have private income greater than \$50 per week, the proportion of families in this situation is considerably higher:

- Couples with children (69%);
- Sole parents with 3 or more children (52.0%); and
- Sole parents with 1 or 2 children (48.8%).

Table 5: Proportion of RA recipients by household type with private income >\$50 per week, December 2000

Household type	Recipients with private income		
	All recipients	#	%
Singles sharing	128,111	22,709	17.7
Single person (independent)	345,604	50,524	14.6
Couple	65,432	23,516	35.9
Sole parent with 1 or 2 children	176,016	85,872	48.8
Sole parent with 3+ children	31,651	16,460	52.0
Couple with 1 or 2 children	99,921	69,392	69.4
Couple with 3+ children	41,651	28,875	69.3
Total	888,386	297,348	33.5

Source: Data provided by the Commonwealth Department of Family and Community Services

(3) RA recipients by type of Centrelink payment

Most RA recipients also receive a Centrelink pension or allowance, and some recipients of these will also be receiving Family Tax Benefit (see Table 6). The largest payment types are:

- Newstart Allowance (24.5%);
- Parenting Payment (single) (20.7%);
- Disability Support Pension (17.2%); and
- Age Pension (16.8%).

However, the picture changes considerably for RA recipients whose private income is greater than \$50 per week. The two major payment types are:

- Parenting Payment (single) (28.0%); and
- Family Tax Benefit (27.5%).

Table 6: Number and percentage for type of Centrelink payment, all RA recipients and recipients with private income >\$50 per week, December 2000

Type of Centrelink payment	All recipients		Recipients with private income >\$50 per week	
	#	%	#	%
Youth Allowance	71,583	8.1	18,127	6.1
Newstart Allowance	217,797	24.5	34,268	11.5
Age Pension	149,582	16.8	39,285	13.2
Disability Support Pension	152,866	17.2	18,945	6.4
Parenting Payment (partnered)	31,241	3.5	21,599	7.3
Parenting Payment (single)	183,546	20.7	83,353	28.0
Family Tax Benefit	81,771	9.2	81,771	27.5
Total	888,386	100.0	297,348	100.0

Source: Data provided by the Commonwealth Department of Family and Community Services

While, overall, 33.5% RA recipients have private income greater than \$50 per week, Table below indicates that the incidence varies considerably between payments types with the largest incidence among those receiving:

- Family Tax Benefit (100% – by definition);
- Parenting Payment (partnered) (69.1%); and
- Parenting Payment (single) (45.4%).

On the other hand, those receiving Disability Support Pension and Newstart Allowance have a low incidence of private income greater than \$50 per week, at 12.4% and 15.7% respectively.

Table 7: Proportion of RA recipients by type of Centrelink payment with private income >\$50 per week, December 2000

Type of Centrelink payment	All recipients		Recipients with private income >\$50 per week	
	#	%	#	%
Youth Allowance	71,583		18,127	25.3
Newstart Allowance	217,797		34,268	15.7
Age Pension	149,582		39,285	26.3
Disability Support Pension	152,866		18,945	12.4
Parenting Payment (partnered)	31,241		21,599	69.1
Parenting Payment (single)	183,546		83,353	45.4
Family Tax Benefit	81,771		81,771	100.0
Total	888,386		297,348	33.5

(4) *RA recipients by household type and type of Centrelink payment*

Table outlines major RA recipients by household type and type of Centrelink payment:

- Sole parents with 1 or 2 children receiving Parenting Payment (single) (17.3%);
- Single persons living alone receiving a Disability Support Pension (13.5%);
- Single persons living alone or sharing, receiving Newstart Allowance (10.8% and 8.1% respectively); and
- Couples with 1 or 2 children receiving Family Tax Benefit (5.0%).

If we consider recipients who have private income greater than \$50 per week, the picture changes considerably. The major groups are:

- Sole parents with 1 or 2 children receiving Parenting Payment (single) (23.1%);
- Couples with 1 or 2 children receiving Family Tax Benefit (15.0%);
- Single persons living alone receiving Age Pension (8.4%);
- Couples with 3 or more children receiving Family Tax Benefit (6.4%);
- Sole parents with 1 or 2 children receiving Family Tax Benefit, couples with 1 or 2 children receiving Parenting Payment (partnered), and sole parents with 3 or more children receiving Parenting Payment (single) (5.5%, 5.2% and 5.0% respectively); and
- Singles sharing receiving Youth Allowance, and couples receiving the Age Pension (each 4.1%).

While, overall, 33.5% of RA recipients have private income greater than \$50 per week, the final column of Table indicates that the incidence varies extensively between different household types and Centrelink payment types:

- All families receiving Family Tax Benefit (by definition);
- Couples with 1 or 2 children, or with 3 or more children receiving Parenting Payment (partnered) (68.8% and 69.9% respectively); and
- Sole parents with 1 or 2 children, or with 3 or more children receiving Parenting Payment (single) (44.5% and 50.1% respectively).

Table 8: RA recipients by household type and type of Centrelink payment, all recipients and recipients with private income >\$50 per week, December 2000

Household type and type of Centrelink payment	All recipients		Recipients with private income >\$50 per week		% Household and Centrelink payment type
	#	%	#	%	
Singles sharing	128,111	14.4	22,709	7.6	17.7
Age Pension	12,986	1.5	2,035	0.7	15.7
Newstart Allowance	72,009	8.1	8,621	2.9	12.0
Youth Allowance	43,116	4.9	12,053	4.1	28.0
Single person	345,604	38.9	50,524	17.0	14.6
Age Pension	104,505	11.8	24,857	8.4	23.8
Disability Support Pension	120,214	13.5	9,632	3.2	8.0
Newstart Allowance	96,308	10.8	11,498	3.9	11.9
Youth Allowance	24,577	2.8	4,537	1.5	18.5

Table 8: RA recipients by household type and type of Centrelink payment, all recipients and recipients with private income >\$50 per week, December 2000 (continued)

Household type and type of Centrelink payment	All recipients		Recipients with private income >\$50 per week		% Household and Centrelink payment type
	#	%	#	%	
Couple	65,432	7.4	23,516	7.9	35.9
Age Pension	31,105	3.5	12,162	4.1	39.1
Disability Support Pension	17,690	2.0	5,329	1.8	30.1
Newstart Allowance	14,001	1.6	4,769	1.6	34.1
Youth Allowance	2,636	0.3	1,256	0.4	47.6
Sole parent with 1 or 2 children	176,016	19.8	85,872	28.9	48.8
Age Pension	414	0.0	56	0.0	13.5
Disability Support Pension	4,184	0.5	703	0.2	16.8
Newstart Allowance	969	0.1	167	0.1	17.2
Parenting Payment (single)	154,019	17.3	68,572	23.1	44.5
Youth Allowance	62	0.0	6	0.0	9.7
Family Tax Benefit	16,368	1.8	16,368	5.5	100.0
Sole parent with 3+ children	31,651	3.6	16,460	5.5	52.0
Disability Support Pension	447	0.1	105	0.0	23.5
Newstart Allowance	123	0.0	20	0.0	16.3
Parenting Payment (single)	29,527	3.3	14,781	5.0	50.1
Family Tax Benefit	1,554	0.2	1,554	0.5	100.0
Couple with 1 or 2 children	99,921	11.2	69,392	23.3	69.4
Age Pension	572	0.1	175	0.1	30.6
Disability Support Pension	7,482	0.8	2,401	0.8	32.1
Newstart Allowance	23,423	2.6	6,291	2.1	26.9
Parenting Payment (partnered)	22,606	2.5	15,562	5.2	68.8
Youth Allowance	1,136	0.1	261	0.1	23.0
Family Tax Benefit	44,702	5.0	44,702	15.0	100.0
Couple with 3+ children	41,651	4.7	28,875	9.7	69.3
Disability Support Pension	2,849	0.3	775	0.3	27.2
Newstart Allowance	10,964	1.2	2,902	1.0	26.5
Parenting Payment (partnered)	8,635	1.0	6,037	2.0	69.9
Youth Allowance	56	0.0	14	0.0	25.0
Family Tax Benefit	19,147	2.2	19,147	6.4	100.0
Total	888,386	100.0	297,348	100.0	33.5

Source: Data provided by the Commonwealth Department of Family and Community Services

(5) Overall assessment

Table summarises the characteristics of major groups of RA recipients. It highlights the household type and Centrelink payment type of those who have private income greater than \$50 per week compared with all RA recipients. The table also shows the household type and type of Centrelink payment of those groups with the highest incidence of private income greater than \$50 per week, compared with the characteristics of major groups of RA recipients with private income greater than \$50 per week.

Based on this modelling, it can be safely concluded that a CHO seeking to utilise private sector investment should target the following groups:

- Sole parents with 1 or 2 children receiving Parenting Payment (single)
- Couples with 1 or 2 children or with 3 or more children receiving Family Tax Benefit
- Single persons living alone on the Aged Pension.

Targeting these groups represents the best chance CHOs have of finding tenants who can support private sector investment. It is notable that while single persons living alone and single persons sharing, particularly those receiving Disability Support Pension or Newstart Allowance are the largest groups overall in receipt of rent assistance, they are not the groups which have private incomes sufficient to support private sector investment. (Other data may indicate that these groups operate between two extremes – they are on full pension or allowance or they are working to such an extent that they are not longer eligible for any Centrelink payment, including rent assistance).

However, a CHO could include single persons living alone on the Aged Pension as a target group. While the data indicates that the size of this group is considerably lower than sole parents and couples with children (representing 8.4% of RA recipients with private income greater than \$50 rather than 23.1% and 15.0% respectively), a CHO could expect it to grow: the number of aged persons receiving RA recipients can be expected to grow as a result of demographic changes, and; the proportion of aged persons with private income can be expected to grow as the Superannuation Guarantee impacts on retirement incomes.

A CHO could minimise their risk of future changes in income by targeting those groups with the highest incidence of private income greater than \$50 per week, viz. families, both Couples and Sole Parents receiving Family Tax Benefit or Parenting Payment. While other groups such as singles living alone receiving the Aged Pension, singles sharing receiving Youth Allowance and couples receiving the Aged Pension are large groups overall, the incidence of private income greater than \$50 per week is lower and thus the risks of targeting this group are higher.

Table 9: Summary of characteristics of major groups of RA recipients, December 2000

Overview	Household types		Type of Centrelink payment		Household type and Centrelink payment		
	Major groups	High Incidence	Major groups	High Incidence	Major groups	High Incidence	
All RA recipients	Single persons alone		Newstart Allowance Parenting Payment Disability Support Pension Age Pension		Sole parents with 1 or 2 children receiving Parenting Payment (single) Single persons living alone receiving a Disability Support Pension Single persons living alone or sharing receiving Newstart Allowance Couples with 1 or 2 children receiving Family Tax Benefit		
Private income greater than \$50 per week	33.5%	Sole parents with 1 or 2 children Couples with 1 or 2 children Single persons (sharing or living alone)	Couples with children Sole parents with 3 or more children Sole parents with 1 or 2 children.	Parenting Payment (single) Family Tax Benefit	Family Tax Benefit (by definition) Parenting Payment (partnered) Parenting Payment (single)	Sole parents with 1 or 2 children receiving Parenting Payment (single) Couples with 1 or 2 children receiving Family Tax Benefit Single persons living alone on the Age Pension Couples with 3 or more children receiving Family Tax Benefit Sole parents with 1 or 2 children receiving Family Tax Benefit Couples with 1 or 2 children receiving Parenting Payment (partnered) Sole parents with 3 or more children receiving Parenting Payment (single) Singles sharing receiving Youth Allowance Couples receiving the Age Pension	All families receiving Family Tax Benefit (by definition) Couples with 1 or 2 children or, with 3 or more children receiving Parenting Payment (partnered) Sole parents with 1 or 2 children or, with 3 or more children receiving Parenting Payment (single)

4. A FINANCIAL PRODUCT AND INVESTMENT VEHICLE FOR RETAIL INVESTORS

Stage 2 of this Project explored the parameters within which a CHO operates. The next stage, reported in this section, was to explore the characteristics and expectations of private retail investors and to develop a financial product and investment vehicle through which private retail investors could invest in community housing. This was undertaken in conjunction with Macquarie Bank.

This section begins with a discussion of private retail investors and their expectations, then outlines the brief provided by the Project team to Macquarie Bank, their response to the brief, and their assessment of the proposed financial product and investment vehicle. It concludes by outlining an alternative approach proposed by Macquarie Bank.

4.1 Retail investors

Broadly speaking, we can distinguish between two types of retail investors. The first are classic investors, those who are motivated largely by their expectations of after-tax returns and who make decisions rationally on the basis of considerable research. After-tax returns are their primary concern because this is the benefit they will derive from the investment. Different investments have different risks, and investors will expect greater returns where they believe that the risks are greater. The risks may relate to the skills of the manager or to a perception that low income tenants tend to default more on rent or that the government may change its policies and thus the capacity of tenants to pay rent. This type of retail investor considers a range of investments (including the private rental market) and determines their investment choices on a risk/return basis.

The second type of retail investor is motivated by a broad range of factors, only some of which are financial. Some have inherited a property and lease it out while deciding its future. Others prefer to invest in 'bricks and mortar' rather than in financial products, not because the returns are greater, but because they believe bricks and mortar to be more reliable and real. Also included in this group are investors who buy property not solely for financial reasons, but because they can put their own handyman skills to work and thereby build up their own sweat equity while receiving rental income.

The contrast between these two types of investors highlights the major difficulty in developing a financial product and investment vehicle for community housing. As Macquarie Bank explains:⁶

Investors would normally invest in residential property for reasons including potential for capital growth, access to ongoing yield, capital security (real or perceived), availability of tax benefits, ability to actively manage and improve properties, emotional motivations and control over realisation (albeit that liquidity is constrained by property market inefficiencies and high transaction costs). Macquarie's view is that an investment in the Pooled Fund would need to replicate as closely as possible the characteristics of an investment in residential property in order to maximise its chances of attracting investors...

The Pooled Fund interposes itself between the investor and the property thereby removing the direct (emotional) attachment to, control over and perceived ability of owners to influence the value of the property that are commonly articulated reasons for investors' prima facie willingness to accept lower returns on residential housing investment than are available from alternative investments. Institutional arrangements for example, between the CHOs and the Pooled Funds, can probably only ever partially address these issues.

Retail investors in the private rental market are willing to accept lower returns for 'emotional' reasons. They may be unaware of the relative costs and benefits of private rental investment compared with other financial products. Attempts to shift a retail investor in private rental to an alternative product providing equivalent returns will be difficult. It involves an increasing awareness of the returns on private investment and competition from an array of other financial products.

⁶ See Appendix II.

4.2 Brief to Macquarie Bank

The Project team developed a brief to Macquarie Bank (see Appendix I). This set out the parameters confronting CHOs and was provided to inform the investment professionals commissioned to design the product vehicle. The brief was developed around a proposal for a CHO to utilise private retail investment to acquire dwellings over a five-year period in Melbourne. The brief:

- Provided an **introduction** to the Project and the brief;
- Provided **background information** on community housing and CHOs;
- Proposed a **target group** for dwellings as families and couples with incomes in the range of \$30,000 to \$40,000 per annum;
- Proposed particular **social objectives** for the housing project;
- Proposed a housing project on a **scale** which would acquire 300 dwellings (180 x 2-bedroom units and 120 x 3-bedroom units);
- Proposed medium density units as the **form of housing**;
- Proposed a **location** in which to acquire units – inner and middle rings of Melbourne – and estimated the prices of these dwellings;
- Outlined the **capital requirements** of the housing project;
- Proposed real annual **capital growth** in dwelling values ranging from 0.5% to 1.5% with an overall average of 1.0%;
- Estimated **rent revenue** based upon gross rental yield of 6.0% for inner Melbourne and 6.5% for the middle ring;
- Outlined **property and tenancy management** arrangements;
- Outlined **operating costs** for dwellings;
- Outlined **asset management** arrangements;
- Indicated the type of **investors** sought, viz. retail investors;
- Indicated the most likely form of **government support**, if required;
- Outlined the nature of the advice sought on a **financial product and an investment vehicle**; and
- Sought advice on the sensitivity of the product to changes in the market (rent revenue and capital growth) and the scale of the project.

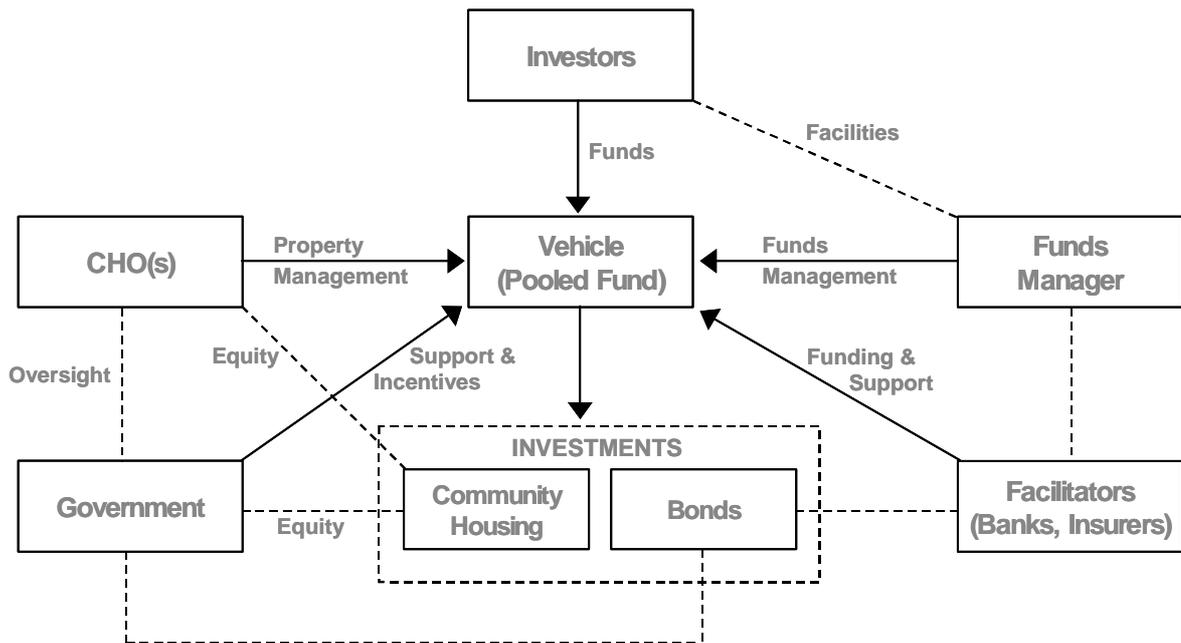
4.3 Proposed financial product and investment vehicle

Macquarie Bank responded in two ways (see Appendix II). They proposed a retail investment vehicle for community housing. However, in their assessment of this, they considered that ‘the risks, costs and rigidity of a Pooled Fund are likely to outweigh any benefit that it may provide as a source of significant funds for community housing’. They then proposed an alternative approach. The former is discussed in this section, while the latter is discussed in Section 4.5.

Diagram 2 outlines the proposed vehicle and the inter-relationship and roles of other participants. The major participants are:

- Investors who provide funds;
- CHOs which, on a fee-for-service basis, manage the properties (both tenancy management and asset management) on behalf of the Pooled Fund and may provide equity funds for joint ventures with the Pooled Fund. In addition, they may provide other services such as property acquisition, project development, and oversight of returns to investors;
- Government which provides support to the Pooled Fund through incentives for investors and equity funds for joint ventures or even invests in the Pooled Fund;
- Funds manager who manages the funds raised by the Pooled Fund: this includes investment review and negotiation, funds management, accounting and reporting requirements, promotion, funds and investor administration, and arranging financing for the Pooled Fund and for the investors; and
- Facilitators such as banks, underwriters and insurers which provide funding and support to the Pooled Fund.

Diagram 2: Proposed vehicle for investing in community housing and inter-relationships and roles of participants



Akin to a listed property trust, this type of vehicle would facilitate investor familiarity and optimise tax efficiencies. A single class of securities is proposed with funds allocated at the housing project level between the various interested parties. Investment in the Fund would be of an equity nature in order to replicate as closely as possible direct investment in residential property.

Both CHOs and governments could invest directly in community housing projects alongside the Pooled Fund or, alternatively, governments could invest in the Pooled Fund itself.

Finally, Macquarie Bank notes that while there are precedents for this type of vehicle in the investment market in the listed property trust sector (usually commercial and retail property trusts) and infrastructure sector, there are no international precedents in community housing. Given more mature community housing systems and a more sophisticated approach to capital raising in other countries, this suggests that a Pooled Fund may have difficulties successfully operating in Australia.

4.4 Assessment of the proposed financial product and investment vehicle

In assessing the proposed investment vehicle, Macquarie Bank considered a number of elements.

First, the Pooled Fund can be distinguished from direct investment in residential property in a number of ways. It interposes itself between the investor and the property, and thus the direct attachment which a retail investor has with 'bricks and mortar' is broken. While this may not impact on the level of returns, a Pooled Fund is one among many types of investments which an active and discerning investor may consider, and thus their expectations of return tend to be higher. While the liquidity of investment is similar to residential investment, it is less than in other financial products. The Pooled Fund provides some important benefits. It allows the opportunity to invest in residential property with lower capital outlays required.

Second, Macquarie Bank considered the investment parameters for the Pooled Fund. Their analysis suggested that 'sophisticated investors in property require a pre-tax return in excess of 10.0% p.a.'. However, based on the assumptions outlined in the brief prepared by the Project team, Macquarie Bank estimated that the pre-tax return and pre-tax internal rate of return (which includes capital growth) on the Pooled Fund for community housing are in the order of 3.0% p.a. (and growing at the rate of inflation) and approximately 6.0% p.a. respectively. On this basis, the Pooled Fund would require significant subsidies if commercial rates of return are to be achieved.

Third, their view is that ‘the primary investor class for the Pooled Fund would be social investors’, i.e. those who are prepared to accept a lower rate of return for an investment in a social good. This is a relatively small class of investors. However, as returns are enhanced through subsidies from government, it is expected that their size would grow.

Macquarie Bank conclude as follows:

The implication...is that the establishment of a successful Pooled Fund for investment in community housing is likely to depend on one or a combination of the following:

- *Access to a broad group of readily identifiable social investors; and*
- *Subsidising of returns via government or other support and incentives or CHOs funds (perhaps originating from equity accumulated in current projects).*

Macquarie considers that the risks, costs and rigidity of a Pooled Fund are likely to outweigh any benefit that it may provide as a source of significant funds for community housing.

4.5 An alternative proposal for private investment in community housing

Macquarie Bank also considered an alternative approach which builds upon the strengths of private rental investment as a ‘cottage industry’. This seeks to recognise a variety of motivations for private rental investment in an industry which is not always driven by the desire to maximise financial returns.

This alternative approach is to provide financial incentives for investors in the private rental market to lease dwellings to CHOs. Macquarie’s particular proposal is a tax exemption on a proportion of rental income (for example, 20%) where the owner leases a dwelling to a CHO for a minimum period of, say, five years. The level of this incentive could be varied over time in order to ensure a regular supply of stock at minimum cost to government.⁷

Furthermore, Macquarie believes that this will not only provide incentives for investors in the current cottage industry but also has the potential to encourage new investment in cluster and larger-scale developments.

⁷ The policy implications of this alternative approach are discussed below.

5. POLICY IMPLICATIONS

The research undertaken as part of this Project has a number of policy implications. These form the subject matter of this section. The first sub-section reflects upon the policy implications for community housing while the second sub-section discusses some broader implications for the private rental sector and social housing more generally.

The characteristics of different residential property markets can vary considerably from those proposed in the assumptions for this Project. Thus, it is possible that investors can make adequate returns from investment in particular properties at particular times and in a particular private rental market. The assumptions underpinning the broad conclusions of this report tend to reflect averages across a range of markets, rather than particular markets. Where an organisation seeks to invest in the residential rental market across a number of markets, then their returns are more likely to reflect the conclusions of this report. However, individual retail investors with good local knowledge may be able to pick individual properties in particular markets with some success, particularly in relation to expectations of capital gains.

5.1 Policy implications for community housing

Despite substantial policy reform over the last twenty years, Australia is still characterised by high levels of unmet housing need, including homelessness (Affordable Housing National Research Consortium 2001). Contributing to this has been two decades of under-investment in social and affordable housing (Wulff, Yates and Burke 2001). This Project began with the hope of developing a financial product and investment vehicle through which private retail investors could provide capital for community housing, thereby alleviating some of these pressures.

The research has, unfortunately, provided little optimism for the future. The literature, the experience in other countries and advice from the finance industry all indicate that such investment is unlikely without higher levels of government support and subsidy.

(1) No private investment in community housing without government intervention

Retail investors are currently still active in the private rental market. For a variety of mainly non-financial reasons, they appear to be willing to invest directly in the residential property market. However, if, as proposed, a vehicle is interposed between the retail investor and 'bricks and mortar', it appears highly unlikely that returns will be sufficient to attract funds from this same group of investors, even if the returns are equivalent to that in the private rental market.

If CHOs are to utilise private retail investment for the expansion of community housing, then some form of additional government intervention is necessary. This could take the form of capital subsidies (in the form of free equity) or operating subsidies directly to CHOs (in addition to RA). At the Commonwealth level, there could be changes in capital gains and income tax provisions or taxation concessions. At the state level, there could be land tax exemptions, stamp duty exemptions, council and water rate concessions etc. No one arrangement is probably sufficient to enable a CHO to break even.

(2) Capital funds from government are necessary

The research has highlighted the extent to which many of those dependent on a Centrelink payment are only able to afford rents that cover the operating costs of providing community housing. Indeed, the income of some groups such as young people are inadequate to meet even operating costs. Without a continuing stream of capital subsidies or free equity, or without a substantial boost to benefit levels, these households will continue to be vulnerable to extreme housing stress.

(3) The target group for CHOs utilising private sector investment

Private sector investment in community housing will only be financially feasible for CHOs targeting low income households that receive some private income in addition to their Centrelink payments. The maximum proportion of private capital that can be supported will vary according to local circumstances. This proportion reduces as the extent of private income reduces and the price of houses increases.

(4) Cost-effective private sector investment

The most cost-effective schemes for attracting private sector investment are likely to be those which most closely approximate the existing private rental market where expectations of returns are low by comparison to more sophisticated vehicles with a similar risk profile.

The Macquarie Bank, in its alternative approach, builds upon the strengths and characteristics of the current cottage industry. Rather than trying to shift investors out of the private rental sector, it proposes financial incentives for investors in the private rent market to lease dwellings to CHOs. Further work still needs to be done on the nature and level of the incentive, but this approach suggests a direction for further exploration.

(5) Key role for CHOs

The best way to attract private investment into a form of housing which guarantees outcomes for tenants is through a financial incentive which is linked to an accredited CHO. This is a key component of Macquarie Bank's alternative approach.

The role of accredited CHOs in this alternative approach has a number of implications. First, it works to address one aspect of the problem recently identified by Wulff, Yates, and Burke (2001): that much of the private rental stock at the low end of the market is occupied by higher income groups.

Second, eligibility for these financial incentives can be limited by linking it to CHOs which are registered under any future legislative requirements. In addition, these Commonwealth tax concessions could be linked with requirements on state government to exempt these dwellings from land tax and to make them eligible for council and water rate concessions.

Finally, CHOs could build the capacity to negotiate long-term leases with appropriate reductions from market rents for housing management, vacancies and bad debts, and possibly maintenance, rates and insurance.

(6) The form of the financial incentive

The most simple and manageable form of financial incentive is likely to be a tax exemption on a proportion of the income derived from investment. This form of financial incentive recognises the nature of the private rental sector as a cottage industry and builds upon this. It is also a form of incentive which can be adjusted according to the level of supply at any one time. Further work still needs to be done on the level of this incentive and how the adjustments might occur.

(7) Community housing tenants continue to remain eligible for RA

CHOs can utilise some retail investment for community housing. However, this is highly dependent upon maximising the extent to which they can capture RA. They can only do this if community housing tenants continue to be eligible. Moreover, any change to the structure which reduces CHOs' capacity to capture RA will undermine their capacity to utilise private retail investment and put at risk any investment already undertaken.

(8) Alternative rent setting policies

In order for CHOs to manage schemes involving private sector investment, including Macquarie Bank's alternative approach, it will be necessary to adopt alternative rent setting policies which provide greater predictability in their rental income. Such policies are only necessary where the CHO is utilising private sector investment and thus where tenants are in receipt of relatively high incomes.

(9) Risk management and CHOs

The utilisation of private sector investment for community housing poses a quantum leap in risks for CHOs. Most are largely unprepared to manage the risks of private sector investment. Many have yet to extend their management capacity beyond tenancy management, let alone property management and asset management. It is only when CHOs have developed these capacities that they may be in a position to take on the much riskier business of utilising relatively high levels of private sector investment.

It is imperative that CHOs implement strategies to enhance their risk management capacities. Initially, they will need to build up considerable expertise in the private rental sector as well as housing finance and housing economics.

A regulatory regime which provides specific accreditation to CHOs utilising private sector investment is necessary to provide assurance to private investors and public accountability. The current review of the National Community Housing Standards needs to develop standards which specifically address private sector investment and the associated risk management requirements.

One attraction of private investment is the increased control which CHOs have in the long term over their housing portfolios. However, as they utilise private investment for the acquisition of community housing, the policy and financial risks will increase considerably. Future autonomy must be weighed against the capacity and skill of a CHO to manage these risks.

5.2 Policy implications for the housing market and social housing

The previous sub-section has focused largely upon the policy implications of the research for community housing. This sub-section shifts the focus to consider the policy implications for both the social housing sector more broadly and the private rental sector.

(1) Reform of the private rental market

Over the past two decades the Commonwealth government has been focusing on improved affordability in the private rental sector with a view to widening the range of choices available to low income households. However, a number of studies have highlighted the weaknesses of this approach (Berry 2000; Wulff, Yates and Burke 2001). The low income private rental housing sector has been slow to respond in terms of both quantity and quality.

The Positioning Paper for this Project has highlighted the nature of private rental investment, in particular:

- That the market is dominated by retail investors owning 1 or 2 dwellings;
- That corporate and institutional landlords are largely absent from the market; and
- That landlords are reluctant to enter into leases longer than 12 months.

A number of studies have also highlighted the relatively unattractive rates of return as a key reason for the absence of institutional landlords (Berry 2000). The private rental market is indeed a cottage industry. In some segments, such as at the most expensive end and for those seeking short-term housing, it operates relatively well (Berry 2000). However, for the most part, it is an industry which falls short in meeting the needs of tenants, in the quality of the services it provides and in providing longer-term tenure. Moreover, as a cottage industry, its future is uncertain as more investors recognise better returns in alternative financial products, its capacity to meet the needs of tenants and to provide quality services in a sustainable way is doubtful, and it appears largely impervious to reform.

A critical issue for reform of the sector and its long-term future is to encourage corporate and institutional landlords into the market. This is most unlikely without significant increases in market rents and subsequent demands for increases in government support for low and middle income tenants. Among the alternatives facing government are:

- Do nothing and so maintain the status quo – the cottage industry – and live with an industry that generally does not meet the needs of tenants and deliver quality services;
- Introduce some reform of the private rental sector – a better focus on tenant outcomes and delivery of quality services – by supporting alternative approaches which combine the strengths of both the private sector and the community sector; and
- Fund and support an alternative housing sector such as the social housing sector where leakage of funds into other activities is very limited.

Macquarie Bank's approach is within the second alternative. It brings together private equity investors and CHOs focused on tenant outcomes and the delivery of quality services. Current developments in the community housing sector – accreditation and a regulatory framework – set the scene for a major reform of the private rental sector. While the private sector provides significant capital for investment in housing, the link with the community sector has the prospect of delivering a better quality of stock, extending security of tenure for tenants and, within an accreditation framework, providing tenants with a quality service.

(2) Private investment in social housing

In the previous sub-section, the importance of government intervention has already been noted. Free equity is particularly important if social housing providers are to target those households whose sole source of income is a Centrelink payment.

However, the analysis in this Project has differentiated between those households who rely solely upon Centrelink payments and those who supplement these with other sources of income. It is households within this latter group who have, to varying levels, a capacity to support private sector investment in social housing. Such investment will more rapidly expand the social housing sector and bring lasting benefits to it.

On the other hand, the Positioning Paper for this Project has highlighted a long history of attempts to utilise private sector investment in community housing, dating back to the early 1980s. This available research confirms that a large volume of investment is needed to meet the ongoing demands for social housing. Current levels are at a historic low. Yet neither the Commonwealth nor the state governments have been able to reach any consensus on a vehicle to deliver private sector funds for social housing purposes. There appears to be a shared view that one national vehicle is the preferred option. It is now critical that they come to some agreement on the arrangements governing this vehicle which will attract private sector funds, and put it in place so that all social housing providers can benefit.

APPENDIX I: BRIEF TO MACQUARIE BANK REGARDING PRIVATE RETAIL INVESTMENT IN COMMUNITY HOUSING

As this Research Project was taking shape, Ecumenical Housing approached Macquarie Bank for their assistance in developing a financial product and investment vehicle through which private retail investors could invest in community housing. They agreed to provide that assistance on a *pro bono* basis.

In the course of the first two stages, the Project team met with Macquarie Bank to discuss progress and a range of issues which we believed important to the development of an appropriate financial product and investment vehicle for private retail investors.

These discussions highlighted the broad range of variables which had to be taken into account in developing this financial product and investment vehicle. In order to make these more manageable for Macquarie Bank and to develop a product and investment vehicle most appropriate to our needs, Ecumenical Housing developed the following brief to Macquarie Bank. The brief attempts to outline a concrete proposal around which Macquarie Bank could develop an appropriate financial product and investment vehicle.

TO: Paul Malan, Director, Investment Banking Group, Macquarie Bank Ltd
FROM: Hal Bisset, Executive Director, Ecumenical Housing Inc
DATE 11 October 2001
RE Brief for private investment in community housing

Introduction

Ecumenical Housing and the Swinburne Institute for Social Research, as part of an Australian Housing and Urban Research Institute research project, are developing a proposal to raise private finance for investment in community housing. The project involves:

- (1) reviewing the literature relevant to the project;
- (2) documenting the parameters of community housing provision to inform investment professionals;
- (3) the development of an appropriate financial product and vehicle to raise private finance;
- (4) writing a final report documenting the outcomes of the project including recommendations in regard to implementation.

This brief sets the parameters for the finance and is provided to inform the investment professionals commissioned to design the product vehicle. The final report will be considered by Commonwealth and state departments responsible for social housing. Ecumenical Housing will promote it specifically with the Victorian Office of Housing.

Background

Community housing is long-term rental housing owned and/or managed by non-government, not-for-profit organisations generally registered as Income Tax Exempt Charities with Public Benevolent Institution Status. The *raison d'être* of community housing organisations (CHOs) is to provide appropriate, secure and affordable housing to low income residents. In general CHOs provide housing for those eligible for public housing. This includes households with incomes in the range of \$10,00 to \$50,000. Over recent years the priority within community housing has been to house the lowest income groups, generally those receiving less than \$30,000 per annum. However, as a result, many households are missing out and subsequently experience significant affordability problems, particularly in inner city areas where rents are high and have been rising rapidly in recent years. Consequently, in this project we are seeking to target those low income households with incomes above \$30,000 per annum who will have some capacity to pay rents which can provide some returns to private investors.

A critical issue is to design a product which does not depend upon the provision of yields greater than currently expected in the private rental market. It is assumed that some form of government support will be provided, however this needs to be transparent and contained. Ongoing subsidies need to be avoided.

Target Group

The target group for dwellings acquired by the CHO will be families and couples with incomes in the range of \$30,000 – \$40,000 (\$575-\$775 per week). Families will consist of both sole parent and couples with 1-3 dependant children under the age of 16 years.

Social Objectives

The aim of the project is to provide housing for low income households which improve their social outcomes vis a vis private rental housing. However it is not the intent to reproduce the specific outcomes of public housing. In particular the social objectives are:

- to improve access to rental accommodation for low income households;
- to provide assurance to tenants in regard to the quality of accommodation;
- to provide higher levels of security of tenure (e.g. 3-5 year leases);
- to enhance affordability for low income households vis-à-vis private rental housing.

Scale of the Project

It is proposed to acquire a portfolio of 300 dwellings. This number is considered to be necessary to achieve management economies. These will include:

180	2-bedroom units
120	3-bedroom units

Form of Housing

It is assumed that all dwellings will be acquired new and that they will be medium density units (town houses and villas). For management purposes it is assumed that the 300 units will be comprised of a minimum of 20 developments ranging in size from 10 units to 50 units.

Location

We expect that 50 per cent of the units will be located in the **middle ring** of Melbourne in suburbs such as Altona, West Footscray, Sunshine, Pascoe Vale, Coburg, Preston, Reservoir, Nunawading, Burwood, Clayton, Oakleigh and Moorabbin. Dwelling prices are estimated to be:

2-bedroom	\$160,000
3-bedroom	\$200,000

The other 50 per cent of units will be acquired in the **inner ring** of the suburbs of Melbourne such as Newport, Yarraville, Footscray, Ascot Vale, Brunswick, Collingwood, Richmond, South Melbourne and Port Melbourne. Dwelling prices are estimated to be:

2-bedroom	\$190,000
3-bedroom	\$250,000

Capital Requirements

Based on the above assumptions we estimate the capital requirements to be:

90 x	\$160,000 =	\$14.4m	
+	90 x	\$190,000 =	\$17.1m
+	60 x	\$200,000 =	\$12.0m
+	60 x	\$250,000 =	\$15.0m
	Total:		\$58.5m

Capital Growth

We expect that the real annual capital growth in dwelling value will range from 0.5% to 1.5%. The average real capital growth for all dwellings is anticipated to be at 1.0%.

Rents

We aim to set affordable rents at 90 per cent of market rent as set out below.

	Middle Ring				Inner Ring			
	Market Rent		Affordable Rent		Market Rent		Affordable Rent	
	Annual	Weekly	Annual	Weekly	Annual	Weekly	Annual	Weekly
2 BR	\$10,400	\$199	\$9,360	\$179	\$11,400	\$218	\$10,260	\$197
3BR	\$13,000	\$249	\$11,700	\$224	\$15,000	\$287	\$13,500	\$259

Market rents are assumed to be 6.5% of market value for middle ring suburbs and 6.0% of market value for inner ring suburbs.

Property and Tenancy Management

Management will be undertaken by either a single newly established CHO or a small number of existing CHOs. Regardless of which management option is decided upon it is assumed they will provide a management service for a fee equivalent to 7 per cent of rental income.

Operating Costs

The CHO will be responsible for meeting all operating costs. The table below presents annual costs according to location and size of dwelling. Some costs are related to the costs of construction rather than the value of dwelling. It is assumed that in the middle ring locations dwelling costs will be 50 per cent of property values while in the inner ring dwelling costs will be 45 per cent of property value.

Where the CHO utilises debt finance to acquire the dwellings it may be necessary to make provision for depreciation, depending upon the level of debt finance. The maximum provision is outlined in the table with a note explaining how the provision is made where debt finance is utilised.

Operating cost assumptions

Type of operating cost	Basis for annual cost	Middle Ring		Inner Ring	
		2BR	3BR	2BR	3BR
Administration	7% market rent	\$728	\$910	\$798	\$1,050
Tenancy management					
Vacancy costs	2% market rent	\$208	\$260	\$228	\$300
Bad debts	0.5% market rent	\$52	\$65	\$57	\$75
Property management					
Rates	0.45% property value	\$720	\$900	\$855	\$1,125
Insurance	0.15% dwelling value [#]	\$120	\$150	\$128	\$169
Responsive maintenance	0.25% dwelling value [#]	\$200	\$250	\$214	\$281
Planned maintenance	0.7% dwelling value [#]	\$560	\$700	\$599	\$788
Total operating costs		\$2,588	\$3,235	\$2,879	\$3,788
Provision for depreciation [^]	2.0% dwelling value [^]	\$1,600	\$2,000	\$1,710	\$2,250

* Market rent is assumed to be 6.0% for inner ring and 6.5% of property value for middle ring

Dwelling value is assumed to be 45% of property value for inner ring and 50% of property value for middle ring

[^] The provision for depreciation will depend upon the equity contribution from government – the formula is: if E^G is greater than BV, then depreciation is 0.9% property value; if E^G is less than BV, then depreciation is $0.9\%PV \cdot E^G / BV$ where E^G is the government's equity contribution and BV is the building value.

Asset Management

The vehicle used to acquire the dwellings and act as the intermediary between investors and CHOs will be expected to acquire the dwellings in a three year period. The costs of acquisition are estimated at \$1M over this period. Depending on the nature of the product there may be ongoing costs for the duration of the investment.

Investors

We assume that this product will be attractive to retail investors interested in a property investment but with insufficient capacity to acquire a 'whole' dwelling, or who are attracted to the 'hands off' nature of this particular property investment, or the capacity to trade without the sale of the dwelling.

Furthermore we expect that the 'social objectives' of the scheme will appeal to 'socially responsible investors' or 'ethical investors' who will subsequently be prepared to make some compromise on returns.

We therefore believe the scheme needs to target ethical investors with \$5K to \$50K to invest in residential property.

Government Support

Both Commonwealth and state governments have articulated considerable interest in private sector investment in social housing. The Commonwealth government, however, has been reluctant to provide any support in addition to existing RA arrangements (approximately \$50 per week to eligible clients of Centrelink). The Victorian government has recently implemented a new program to expand social housing allocating \$94.5M to capital subsidies over three years. We believe that capital subsidies and/or government guarantees from the state government is the most likely form of additional government support.

Product and Vehicle

We are seeking advice on the most appropriate investment product to meet our requirements. We also require advice on the nature of the vehicle best equipped to offer this product, including the costs of managing the vehicle.

Sensitivity

We would also like to be advised on the sensitivity of the product to any changes to:

- (1) the rental income as a proportion of market rents;
- (2) the value of the dwellings;
- (3) the scale of the project.

APPENDIX II: RESPONSE BY MACQUARIE BANK TO BRIEF REGARDING PRIVATE RETAIL INVESTMENT IN COMMUNITY HOUSING

27 November 2001

Mr H Bisset
Executive Director
Ecumenical Housing
20 Queen Street
MELBOURNE VIC 3000
AUSTRALIA

Dear Hal

RETAIL INVESTMENT VEHICLE FOR COMMUNITY HOUSING

Ecumenical Housing and The Swinburne Institute for Social Research (together 'Ecumenical' have asked Macquarie Bank Limited ('Macquarie') to consider the scope for establishing a vehicle investing in community housing which would target retail investors. Such a vehicle would provide a pool of funds which various Community Housing Organisations ('CHOs') could access in order to provide independently appropriate, secure and affordable housing to low income residents. Ecumenical has identified a specific set of possible residents for housing funded by the investment vehicle. Further, Ecumenical has identified investors currently investing in residential housing as being a key investor class primarily because of their apparently lower return requirements than other property investors.

Macquarie considers, on the basis of financial parameters articulated by Ecumenical that it would be difficult to establish an investment vehicle for community housing which would attract broad based retail investor support without significant subsidies. Macquarie has arrived at this preliminary view following a review of relevant, selected literature, consultation with industry participants (especially Ecumenical), analysis of investor requirements and motivations and a survey of international models for funding of community housing.

This letter briefly examines, in turn, the assumptions provided by Ecumenical, a possible structure for an investment vehicle, the parameters that are likely to be required for investors in such a vehicle (and how this compares with what may be available given the assumptions outlined by Ecumenical), the implications of Macquarie's findings and possible alternative approaches that may be adopted.

1. Assumptions

Ecumenical has provided Macquarie with the following assumptions relating to the housing in which the proposed vehicle would invest:

- Affordable rents for tenants would be set at approximately 90% of market rents which are assumed to represent 6.0-6.5% of market value (depending on location);
- Target tenant group for dwellings acquired by the CHOs would be families and couples with incomes in the range of \$30,000-\$40,000 p.a. (and in receipt of Commonwealth Rent Assistance). While not key to the feasibility of the vehicle, it is considered that these tenants are best placed to meet the affordable rents specified for the housing owned by the vehicle;
- The vehicle would reach a size in excess of \$50m within three years investing in developments ranging in size from 10 units to 50 units which would be located in, and equally distributed between, inner ring and middle ring suburbs of major cities;
- Real annual capital growth in dwelling value would range from 0.5-1.5% pa, with average anticipated to be 1.0% pa;
- Specific tenancy management and property costs would represent 1.5-2.0% p.a. of property value;

- Property acquisition costs, assumed to be \$1m over the first three years assuming approximately \$50m of property is acquired; and
- Vehicle establishment and ongoing vehicle management costs, assumed by Macquarie to be \$0.5-\$1.0m and 1.0% of property value respectively.

Macquarie has modelled these assumptions for an unlevered fund in order to determine expected returns to investors (on a pre-tax basis). The key results of this modelling are:

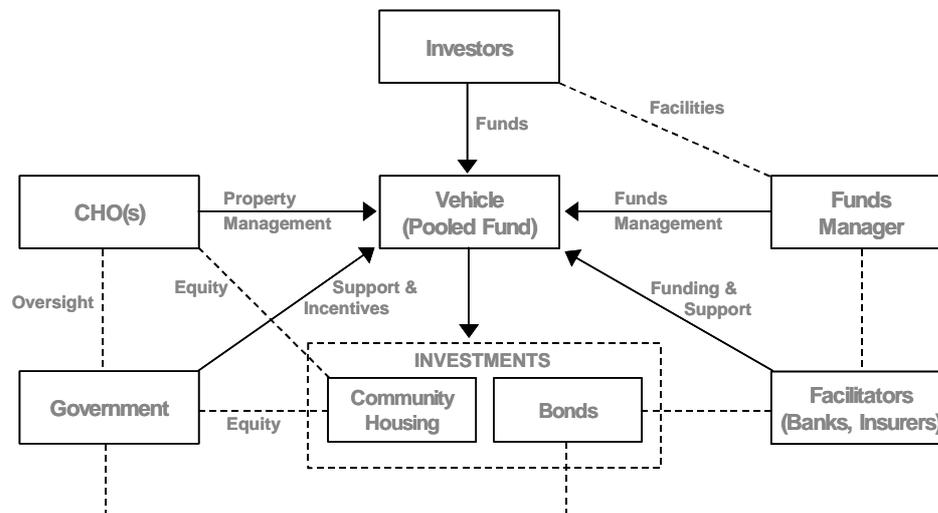
- The vehicle would generate a running, pre-tax, income yield commencing at 3.0% p.a. (and growing at inflation); and
- The pre-tax internal rate of return for the vehicle, i.e. inclusive of capital growth, is estimated at approximately 6.0% pa.

These returns are obviously sensitive to a range of variables, in particular rental yields, operating cost levels, capital growth achieved and investment vehicle size. Nevertheless, discussions between Ecumenical and Macquarie have settled assumptions adopted and the resulting return is considered to be a reasonable central case for evaluation of the economics of an investment vehicle.

2. Investment Vehicle Structure and Arrangements

The diagram below proposes a possible structure for a vehicle investing in residential housing, highlighting the interrelationships, roles and requirements of participants:

The Vehicle ('Pooled Fund') would be established as an umbrella fund from which a range of CHOs could source funds to invest in community housing. In the example above, we have also provided the Pooled Fund with the ability to invest in government bonds and cash thereby allowing it to manage the timing mismatch between availability of funds from investors and the availability of community housing developments for investment as well as the requirement for liquidity to meet investors' redemptions. It is possible that the Pooled Fund may invest in community housing developments alongside CHOs, government or other private sector investors.



It is proposed that the Pooled Fund would be set up as a 'see-through' Trust structure akin to a listed property trust which should facilitate investor familiarity and optimises tax efficiency of the vehicle to investors. For simplicity and, to some degree, for taxation reasons, it is proposed that the Pooled Fund would have a single class of securities although it is possible that other parties, such as government or the CHOs, could hold a different class of securities with different entitlements from those held by external investors. Assuming a single class of securities, returns from community housing projects could be 'sliced and diced' at the project level between various interested parties in order to make the investment attractive from the perspective of the Pooled Fund.

Investors would normally invest in residential property for reasons including potential for capital growth, access to ongoing yield, capital security (real or perceived), availability of tax benefits, ability to actively manage and improve properties, emotional motivations and control over realisation (albeit that liquidity is constrained by property market inefficiencies and high transaction costs). Macquarie's view is that an investment in the Pooled Fund would need to replicate as closely as possible the characteristics of an investment in residential property in order to maximise its chances of attracting investors. This would tend us towards the view that the investment in the Pooled Fund should be of an equity nature. We note that an alternative here would be for investments in the vehicle to be structured to be similar to a bank term account, say, providing 2.5% p.a. return with a high degree of capital security (via insurance of property values) although we consider that such a security is only ever likely to have as its primary market social investors.

Notwithstanding that efforts can be made to approximate a direct investment in residential property with an investment in the Pooled Fund, important distinguishing factors should be recognised:

- The Pooled Fund interposes itself between the investor and the property thereby removing the direct (emotional) attachment to, control over and perceived ability of owners to influence the value of the property that are commonly articulated reasons for investors' prima facie willingness to accept lower returns on residential housing investment than are available from alternative investments. Institutional arrangements for example, between the CHOs and the Pooled Funds, can probably only ever partially address these issues;
- Although, according to Ecumenical, actual returns (net of costs) from direct investment in residential real estate may not differ markedly from the returns likely to be generated from an investment in the Pooled Fund, Macquarie perceives that there may be an expectations gap which derives from, for example, the lack of a true understanding of net returns on the part of direct investors and the benefits which are envisaged from direct control over the asset;
- Liquidity for investors seeking to redeem funds from the Pooled Fund is likely to be constrained, say via a 3-6 month waiting period following notice of intention to redeem, because of the illiquidity of the Pooled Funds underlying investments and the requirement, on the part of the CHO, for the long-term security of tenure. It is noted that inefficiencies in the residential real estate market, for example protracted sale processes and settlement periods, are likely to mean that realisation periods are similar to those proposed for the Pooled Fund;
- Differences in tenant selection, nature of tenants, tenancy arrangements and leasing practices for the Pooled Fund (as compared with 'normal' residential practices) will need to be addressed with acceptable and transparent institutional arrangements between the relevant CHOs and the Pooled Fund which provide investors with the requisite assurity. Note that the services and, potentially, guarantees provided by CHOs could provide investors with a major benefit not readily available in the direct investment market; and
- The establishment and management costs for the Pooled Fund represent a source of value leakage as compared with direct investment, albeit that offsetting benefits could be expected as a result of economies of scale and access to expertise.

A Pooled Fund would, however, offer several potentially important attributes to potential investors:

- The opportunity to invest in a fund offering exposure to the residential property market with a lower required capital outlay and exposure than is possible via a direct investment in housing;
- The ability of the investor to avail themselves of taxation benefits (negative gearing and building allowances) which are typically available for investment properties. In this respect, it is not proposed that the Pooled Fund would gear itself because of the relative cost of funds versus likely returns on housing, risk profile of the CHOs and the ability of investors to gear independently their investments (possibly through facilities arranged by the fund manager);

- Would offer some appeal to social investors, although Macquarie does have reservations about the willingness of social investors to invest in housing being provided to the targeted tenant group (i.e. are they sufficiently worthy of support?) and the depth of the social investor group targeted for the fund, say, those willing to invest a minimum of \$10,000;
- The Pooled Fund would be seeking to benefit from various taxation and other duty concessions available to CHOs, which would be expected to flow through to investors;
- The Pooled Fund would offer the capital (and income) security typically associated with direct investment in real estate. In the context of a Pooled Fund, this could be further enhanced via arrangements with the CHO, government or third parties such as value insurers.

The roles and responsibilities envisaged for parties depicted in the diagram in relation to the Pooled Fund are broadly as follows:

- CHOs would provide, pursuant to detailed contractual arrangements and for a fee enabling them to recover reasonable costs, services including property acquisition, project oversight, property administration, tenancy management, property repair and maintenance and potentially, property warehousing, coinvestment funds and support of returns. CHO arrangements would relate to individual community housing projects.
- The fund manager would, inter alia, undertake investment review and negotiation, funds management activities, fulfil accounting and reporting requirements, promote the Pooled Fund, perform funds and investor administration services and arrange financing for the Pooled Fund (and possibly investors) pursuant to a fee for service arrangement.
- Facilitators, such as Banks, Underwriters and Insurers, may provide funds or support to the Pooled Fund (and possibly investors).
- The role of both Commonwealth and state governments is broad ranging and would encompass providing capital grants for development projects or property acquisitions, providing operating subsidies (say, to CHOs), providing rent assistance to tenants, providing facilitative assistance (such as tax incentives) and prudential oversight, for example of CHOs, to ensure system integrity. For the purposes of the analysis contained in this letter, no additional government support is provided over and above current arrangements, apart from the Pooled Fund being able to directly avail itself of all the concessions available to CHOs.

While there are precedents for these types of arrangements and vehicles in the investment market, for example in the listed property trust and infrastructure sectors, Macquarie has not found any international precedents relating to community housing. While not conclusive, the absence of comparables in markets which, in some cases exhibit more developed capital markets, maturer community housing systems and, possibly, greater cultures of benevolence than Australia suggests potential difficulties.

3. Investment Parameters and Investor Classes

Macquarie has considered the level and nature of returns from a Pooled Fund investing in community housing, the sources of financing (debt and equity) for real estate and the return and other requirements of investor classes, having regard to alternative investments available.

MBL modelling, summarised in Section 1 above, estimates that the annual pre-tax income yield from a Pooled Fund would commence at approximately 3.0% p.a. (growing at inflation) and the total, pre-tax yield (including capital growth) would be approximately 6.0% pa. Ecumenical has indicated that these returns are not materially different from the returns that can be expected by a direct investor in residential real estate.

A relevant benchmark is the construction and head-leasing of residential housing which is undertaken by the Defence Housing Authority (DHA) on long-term Commonwealth government guaranteed leases (say, 5-7 years) for gross yields of 5.0-7.0% p.a. depending

on property characteristics and location. The DHA contracts to undertake property management, repair and maintenance and assures return conditions for a fee of approximately 15% of gross rents. This example suggests that yields from the Pooled Fund are below those of alternative investments, in large part because of the costs of managing and administering the fund itself. Further, Macquarie is not confident that it would be able to attract a material number of investors to the Pooled Fund with similar return requirements to direct investors in residential real estate because of the distinguishing features identified in Section 2 above.

Preliminary analysis by Macquarie of alternative investments suggests that sophisticated investors in property require a pre-tax return in excess of 10.0% p.a. For example, the large and liquid Australian listed property trust market offers investors exposure to higher value and yielding retail, commercial and industrial properties with better credit profiles in return for annual income yields of 7.0-10.0% with potential for capital growth. In order to attain returns of this level, Pooled Fund would require significant (i.e. up to 50%) subsidisation of capital or income (by, say, government or CHOs). At commercial rates of return, the Pooled Fund could, self evidently, be confident of attracting investor support. It is noted that the levels of subsidisation required for the fund to reach a commercial level of return are similar to the level of initial, non-income yielding equity that would be required on projects if mortgages on the properties are maximised (having regard to their income generating potential).

Based on the above analysis, Macquarie's preliminary view is that the primary investor class for the Pooled Fund would be social investors. As outlined in Section 2, Macquarie is confident neither of the depth of this grouping amongst retail investors nor the willingness of these investors to contribute funds given possible perceptions of the lack of neediness of the targeted tenant grouping.

Of course, factors such as a high profile media campaign funded by a corporate sponsor or the donation of services or funding which lowered the Pool Fund's cost structure could have a positive impact but the likelihood and extent of these factors is unknown and accordingly not capable of being analysed at the present time. As the return of the vehicle is enhanced, through government or some other subsidisation for example, the field of potential investors would increase along a spectrum until commercial returns are offered. It should be noted that the track record of the fund is going to be important for retail investors and would be an issue for the fund in its formative stages.

Finally, there is a major class of retail investors seeking investment products which provide them with tax advantages. The Pooled Vehicle would offer investors the opportunity to negatively gear as well as a significant amount of the income being tax advantaged. This could be further enhanced if, say, investors could benefit from the tax status of CHOs as charities or received further concessions on assess ability of income. For example, consider a case where an investor subscribed part of their funds directly into the Pooled Fund with the remainder being in the form of a tax deductible 'donation' to the CHO which could then use the donated funds to subscribe for non-income yielding equity. Issues associated with such structures have not been considered further because of their requirement for government cooperation.

4. Implications and Alternative Approach

The implication from the above analysis is that the establishment of a successful Pooled Fund for investment in community housing is likely to depend on one or a combination of the following:

- Access to a broad group of readily identifiable social investors; and
- Subsidising of returns via government or other support and incentives or CHOs funds (perhaps originating from equity accumulated in current projects).

Macquarie considers that the risks, costs and rigidity of a Pooled Fund are likely to outweigh any benefit that it may provide as a source of significant funds for community housing.

An alternative, and possibly less risky approach, would be to utilise the attractive features of the pre-existing 'cottage industry' which exists today in relation to the housing of presumably numerous low income residents in Australia. There are many factors which have led to the growth of this cottage industry over the decades. Many property owners look to acquire one or more additional residential properties for a variety of reasons including:

- It is seen as a secure asset;
- It can be the subject of negative gearing;
- The owner is prepared to either maintain the property himself or otherwise arrange for its maintenance;
- The owner may have in mind an alternative use for the property in the years to come (as a possible residence for members of his family or even himself as his requirements change);
- It is an asset that can be seen and that one can take pride in.

Importantly, the industry is not at all necessarily driven by the desire to maximise financial returns. This is one of the reasons why property trusts, whilst competitive in the office, retail and industrial sectors, do not appear to be competitive in the residential sector.

The net result is that this cottage industry is a source of housing, some of which is inevitably made available to lower income families and individuals. In accepting that this cottage industry is well established, an alternative approach that we believe is worth considering is to take advantage of this industry and to grow it further, for the benefit of low income tenants, by way of relatively modest government subsidies.

One could, for example, envisage that if an owner agreed to make a residential property available for the use of a low income tenant on certain terms and conditions and the Commonwealth government was willing to exempt a proportion of the rent received from being taxed, then the existing cottage industry could be expanded, possibly quite considerably.

This might work as follows:

- The owner is required to make the residence available to low income tenants;
- A tax exemption as to, say, 20% of the rental income received is available if:-
 - The residence is made available for a minimum period of, say, five years;
 - The owner agrees to a CHO overseeing the leasing arrangement including approving that the residence is appropriate and makes, say, twice yearly inspections to ensure that various minimum standards are adhered to.

There are presumably other ways in which the government incentive could be provided such as accelerated depreciation. Furthermore, the various state governments would also provide incentives by way of reductions in land tax and the stamp duty payable on the acquisition of the relevant property.

It is difficult to be scientific about how much incentive is required to achieve a meaningful result. We believe that a modest income tax exemption of, say, 20% of the relevant net rental stream would send a very powerful message to this existing cottage industry which would result in a not insignificant and measurable increase in its scale. Indeed, an exemption as low as 10% may also provide a significant exemption if combined with appropriate state government taxation and/or stamp duty relief. But, rather like the Commonwealth government's First Home Owner's Scheme or, indeed, the Reserve Bank's ongoing management of interest rates, it may be necessary, over time, to increase or decrease the amount of the incentive package to optimise its effectiveness having regard to the actual cost to the government sector.

We would also see the cottage industry expanding in the sense that the interest in larger, cluster developments for lower income persons might be stimulated. Whilst, a developer of such a cluster might, at the end of the day, obtain a better return through a pure commercial development, he might feel that the government was assisting his desire to give something back to the community. Such a developer may be motivated by incidental factors such as the ability to name the cluster development and to be identified with a good cause (although one

would need to ensure that this was not demeaning to the residents). Presumably, the development could also be sold for a full commercial price after the minimum period during which it had to be made available for low income housing.

As far as marketing is concerned, we do not pretend to be experts in this area but we would say that the enacting of any tax legislation to grant the exemption would be a very powerful 'kick-off' (and even more so if it was the subject of a joint Commonwealth and state government programme of incentives) and it may be that marketing could be very much self generating. It goes without saying that there is little, if any, formal marketing associated with the existing cottage industry.

In summary, the concept behind this alternative approach is to take advantage of what already exists and, with relatively modest subsidies, make it significantly larger for the benefit of low income residents. Furthermore, the existing cottage industry could be improved by, in effect, incentivising owners to subject themselves to sensible regulation by CHOs. In other words, an additional objective would be to raise existing standards of accommodation for low income tenants.

If you wish to discuss the contents of this letter, please do not hesitate to contact me on 9635 8100.

Yours faithfully
Macquarie Bank Limited

Simon McKeon

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