Policy options for stimulating private sector investment in affordable housing across Australia
Stage 1 Report: Outlining the Need For Action

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For the
Affordable Housing National Research Consortium

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Executive Summary

This report presents the findings of stage 1 of a larger project looking at ways of encouraging greater private sector involvement in the provision of affordable housing in Australia. The report:

- Documents the nature and scale of the housing affordability problem in Australia, concentrating on the period since the mid-1980s;
- Notes factors responsible for the intensification of affordability problems and housing stress during this period;
- Identifies the current barriers to private sector and non-government finance for affordable housing, and;
- Outlines recent and continuing changes in the public policy environment, relevant to the challenge of improving housing affordability.

1 Trends in Affordability

The report reviews trends in the key variables influencing housing affordability – notably, labour market participation, inflation rates, household incomes, real interest rates, dwelling prices and rents. The analysis concentrates on three metropolitan regions – Adelaide, Melbourne and Sydney – for which full and consistent data sets were available. These cases also offer useful comparisons across the full range of housing outcomes, both between and within the cities. In the case of Brisbane, Perth and Hobart it was not possible to extract data in a suitable form for comparison over the period chosen with respect to housing affordability. However, these latter cities are included in the analysis of increasing housing stress at the metropolitan level.

Key findings are:

- Nominal mortgage interest rates have fallen progressively through the 1990s. Real rates are also down to below 5 per cent in the current year. Other things equal, housing affordability should increase. However, as we note below, other things have not been equal.

- Median household incomes fell in real terms over the 1986-96 period in all three cities. The fall was greatest for households in the bottom two income quintiles (bottom 40%). By comparison, average weekly incomes rose in line with inflation to 1996 and faster over the last four years. Adelaide real incomes fell more steeply than in Sydney or Melbourne.

- Unemployment has fallen to its lowest level in a decade (more than a decade for Sydney). However, as just noted, household incomes are not keeping pace with inflation suggesting that housing affordability problems may be increasing for people in employment, the so-called working poor.

- The real prices and rents of units and houses increased faster than real incomes in the inner locations of all three cities (except rents in inner Melbourne). The situation further out is more complicated. Fully detached dwelling prices in the outer areas increased faster than average incomes, as did units in outer Sydney. However, unit rents in the other two cities fell in real terms in the outer areas, slightly in Adelaide, significantly in Melbourne. As might be expected, the relative sizes of the increases in real prices and rents were greatest in Sydney.
• Real mortgage payments rose by between 20 and 40 per cent in the two inter-censal periods, 1986-91 and 1991-96, with the largest increases in Adelaide and Sydney in the later period. These increases are clearly fuelled by continuing house price inflation but also probably reflect the impact of changing lending market practices. In particular, the explosion of new mortgage products during the nineties has encouraged a jump in re-financing rates and the opportunity to consolidate other forms of debt. (This fact makes it difficult to interpret affordability trends among purchasing home owners.) Increases in real rents were much more modest across the cities in the 1991-96 period (and slightly negative in Melbourne), perhaps reflecting or reacting to the recession and slow-down in property markets after the late-eighties boom and the faster rate of rent increases in the 1986-91 period.

• The proportion of households renting privately increased significantly during the 1986-96 period in all three cities. This occurred fastest when and where dwelling prices were rising quickest.

• The rate at which purchasing home owners are moving house appears to be falling.

2 Housing Stress

The National Housing Strategy (NHS) defined housing affordability as a situation where ‘housing costs … leave households with a sufficient income to meet other basic needs such as food, clothing, transport, medical care and education.’ Households paying more than 25-to-30 per cent of their incomes in rents or mortgage payments were held to be experiencing affordability problems. Particularly vulnerable, in this view, are low income households who have little left over and little to fall back on to meet basic living costs after paying excessive housing costs. The NHS defined households falling in the lowest two income quintiles, in the overall distribution of income, who pay more than 25 per cent of income in housing costs as being in ‘housing stress.’ That – and the more conservative benchmark of 30 per cent – have subsequently been widely used as an overall measure of housing-related hardship in Australia. More sophisticated benchmarks that recognise the impact of factors other than total gross income have also been proposed. This report uses the conservative (30 per cent) NHS benchmark in analysing the impacts of the trends identified in the preceding chapter on the housing situation of low income tenants in the three cities concerned.

The report focuses on private tenants because the earlier NHS and other research found very low proportions of outright home owners and public tenants to be paying in excess of 30 per cent of their incomes for housing, as well as the difficulties involved in interpreting the discretionary or choice element in the case of purchasing home owners. The most recent housing survey carried out by the Australian Bureau of Statistics (1999) found that the proportion of outright home owners paying more than 30 per cent in housing costs was 4.9 per cent. The figures for purchasing owners, public tenants and private tenants were 27.9 per cent, 9.9 per cent and 54.7 per cent, respectively.

The main conclusions regarding housing stress are as follows.

• Over the 1986-2000 period some areas and dwelling types have become more affordable, and other areas and types less affordable, when all private tenants are taken as a group. For Adelaide, overall, renting and purchasing affordability improved for all dwelling types in the lower income, less central area (Northern Adelaide) but only purchasing, not renting, in the more affluent and central suburbs of Eastern Adelaide. For Melbourne, the situation was similar, with renting and purchasing becoming more affordable in the outer South Eastern region but renting less affordable in inner Melbourne. For Sydney, affordability generally declined across the board for private tenants taken as a whole – with the exception that buying a one bedroom flat in outer-Western Sydney became more affordable.
This mixed situation changes radically when confining attention to the private tenants in the most vulnerable position – ie those in the bottom two income quintiles (bottom 40%). Here the analysis concludes that, in June 2000:

- no households can affordably buy an average (median) priced three bedroom house in any metropolitan location;
- 39% of Adelaide’s and 15% of Melbourne’s salient households can afford to buy an average one bedroom unit in North Adelaide and South East Melbourne (resp.), with no households in Sydney being able to affordably purchase any average one bedroom dwelling in any location;
- only 9% of Melbourne’s, and 3% of Sydney’s salient households can afford to rent an average three bedroom house in South East Melbourne and Outer Western Sydney (resp.), with no households being able to rent an average three bedroom house in any Melbourne location;
- over 50% of salient households from each capital city can afford to rent an average one bedroom unit in the outer locations (North Adelaide, South Eastern Melbourne and Outer Western Sydney);
- a very small proportion of households are able to afford to rent an average one bedroom unit in inner Melbourne or Sydney locations (5%, Inner Melbourne only); and 38% of households can afford the rent of a one bedroom unit in Eastern Adelaide.

To sum up, low income tenants have extremely limited affordable housing choices, both by location and dwelling type. Moreover, where a small degree of choice appears to exist – viz. renting a one bedroom unit on the fringe – this ignores the question of appropriateness. Clearly this only represents a choice for small households.

Housing stress increased substantially for low income tenants over the 1986-96 period:

- Adelaide: up from 63.4% to 76.1%
- Melbourne: up from 60.5% to 74%
- Sydney: up from 67.3% to 80.7%
- Brisbane: up from 63.7% to 64.3%
- Hobart: up from 57.7% to 62.4%

Perth’s proportion fell sightly from 59.9% to 56.1%; Darwin’s proportion fell 7 percentage points to 63.7%

The average for all seven capital cities rose from 64.1% to 72.7%.

The numbers of low income tenants in housing stress increased over the period by 7,400 (Adelaide), 22,600 (Melbourne) and 28,600 (Sydney). The total increase for the seven capital cities was 90,000, so that by 1996, 227,480 low income households were experiencing housing stress, as defined above.

If the housing needs of this large sub-group was met entirely by constructing new dwellings, the estimated total cost is around $27 billion. Recent research estimates that the chronic shortage of low cost rental dwellings in Australia is in excess of 150,000.

By 1996, then, almost three out of four low income private tenants in the main metropolitan areas (excluding Canberra) were suffering housing stress, when measured by the conservative NHS benchmark. The figure was four out of five in Sydney. The increases in real property prices and rents for this group detailed above over the past four years strongly suggests that the proportions of low income tenants in housing stress has further increased.
Stressed renter households are growing much more rapidly than renters as a proportion of all households:

- Adelaide: 69% compared to 26%
- Melbourne: 62% compared to 32.7%
- Sydney: 49% compared to 24.4%
- Hobart: 99.3% compared to 84%; and
- Brisbane: 103% compared to 101.6%.

In Darwin and Perth the rate of growth of stressed households was slightly less than the overall rate of growth for households in the same income categories.

There has also been an increase in the numbers and proportions of higher income households paying more than 30 per cent of their incomes in rent. When added to the bottom 40 per cent group, growth for all tenants in this situation was:

- Adelaide: 55% increase
- Melbourne: 71% increase
- Sydney: 74% increase
- Brisbane: 100% increase
- Perth: 70% increase
- Hobart: 76% increase
- Darwin: 82% increase, and
- a 74% increase across all capital cities.

Some higher income households will choose to commit a higher proportion of their incomes to housing and be able to afford it. However, other tenants may be struggling and reasonably said to be suffering housing stress. This suggests that housing affordability problems may be climbing the income ladder, affecting not only unemployed and under-employed people but those who have been described as the ‘working poor’ and, even middle income households.

If the rate of growth of stressed households experienced in the last 10 years continues, then the number of households experiencing stress in metropolitan Australia will double in 15 years and reach nearly one million within 20 years. This does not include households struggling in regional Australia.

Clearly, existing housing assistance policies are not adequately resolving the problems associated with declining affordability. The Rent Assistance program, in particular, is found to be of very limited effectiveness in both Melbourne and Sydney. This study found that:

- for single persons and couples without children eligible to receive Rent Assistance there is almost no type of (average priced) rental dwelling that is affordable in any local government area in either Melbourne or Sydney;
- Rent Assistance provides no substantial alleviation of housing stress with these family types;
- the number of locations where these households will not experience housing stress has declined significantly since 1994, and Rent Assistance is effective in providing locational choices in a much smaller range of LGA’s in 2000 than in 1994;
- for single persons with one or two children and eligible to receive Rent Assistance, only 1 or 2 bedroom flats are affordable in 48% and 19% of Melbourne LGA’s in 2000, and the number of appropriate locations declined by approximately 50% between 1994 and 2000, for this group. In Sydney only one bedroom flats are affordable in just 20% of locations (i.e.
all other dwelling types are not affordable by this group in any LGA); and, again, the Rent Assistance program was far less effective in widening choice in 2000 than in 1994;

- couples with 1 or 2 children and eligible to receive Rent Assistance have a wider range of locational and dwelling choices than any other group, but only where this group is renting three bedroom housing is Rent Assistance providing greater choices than in 1994;

- as a whole, affordability for pension and benefit recipients has rapidly declined between 1994 and 2000, and Rent Assistance was much less effective in broadening dwelling and locational choices in 2000 than in 1994. Whatever level of effectiveness achieved has been and remains largely confined to family types with children present.

*In other words*, the Rent Assistance program is relatively ineffective in providing either a wider range of dwelling or locational choices for the large majority of recipients in either Melbourne or Sydney. The limited impact of the program on housing affordability has also apparently declined substantially over the second half of the 1990s.

The study also argues that the Rent Assistance Program does not comply with the principals of horizontal equity; similar households in different tenure situations receive different effective levels of housing assistance.

It is also possible that the financial risks associated with the program are more significant than with the alternative supply side option or a mixed demand side-supply side strategy that also includes a leveraged private investment component.

To have maintained the effectiveness of the Program at 1994 levels (limited though it was) would have required a significant increase in the rent cut-off levels and maximum amount of Rent Assistance payable. This in turn would have meant a substantial increase in funding for the Program that would have to be met entirely from Commonwealth funds. To *improve* the effectiveness of the program would require an even larger commitment of Commonwealth funds.

**Extra government funding will indeed be required to deal with the increasing problems of housing affordability in Australia, some of which could usefully be committed to raising the effectiveness of the rent assistance program. However, in order to stretch available government housing subsidy funds further, it would be wise for government to consider ways of leveraging some of those public funds with private funds, as well as expanding rent assistance through the income support system and capital provision through the CSHA. In the light of the various financial and operating risks facing housing authorities, a mixed strategy of delivering the necessary expanding pool of housing assistance through these three main channels – RA, CSHA and leveraged private investment – is most likely to maximise the overall effectiveness of policy on housing affordability and minimise the long term subsidy costs per household assisted. (Stages 2 and 3 of this project develop effective private leveraging options intended to complement the established housing assistance approaches.)**

**In summary**, significant market failure characterises segments of the Australian housing system. This results in inadequate supply responses, especially at the low-cost end of the private rental market due to the small-scale and informal nature of private investment and significant barriers which effectively exclude large scale involvement by institutional investors. Chronic shortages of affordable and appropriate housing for lower income households creates a range of complex negative externalities – i.e. unpriced costs – borne by both the people directly concerned and the community at large. The direct costs of poor housing include adverse impacts on the health and educational opportunities of household members. Impacts on the community include declining social cohesion, loss of social capital, increasing conflict and breakdown or bottlenecks in attracting workers to growing industries. An extreme scenario
would see the social exclusion of a significant section of the population from the normal avenues of participation in society.

This research study strongly suggests that governments and community cannot simply wait for the market to respond. Markets are demonstrably not doing so in this case. Existing government housing assurance policies are not dealing adequately with the problems of declining affordability. There is, therefore, a strong case for policy reform, for new policies aimed at reversing the continuing trend towards less affordable housing in Australia.

3 The Changing Policy Climate

The report points to a number of important policy changes that have occurred over the past decade or so that impinge directly on matters of housing affordability or have implications for attempts to overcome current barriers to greater investment in the provision of more affordable housing. Three main arenas are identified.

Housing Policy.

Housing policy in Australia has been included in the general movement towards market-oriented solutions to social problems and service provision, a common trend in a number of Western countries. This has been evident in the shift of emphasis and government spending away from supply-side housing subsidies towards income support in the form of rent assistance paid through the social security system. Net additions to the public housing stock have fallen in most, if not all States, while expenditure on rent assistance to private tenants is now in excess of $1.6 billion annually. Successive changes to the Commonwealth State Housing Agreement have sought to more clearly delineate Commonwealth and State roles in housing provision. The current policy climate, characterised by significant capital and revenue constraints, has made the State Housing Authorities potentially open to new approaches to asset management that would leverage resources from the private sector. The key issues remain those to do with risk allocation, subsidy policy and political will.

Taxation Reform.

Taxation in its various forms is clearly a major factor in investor decisions about where to invest and in what portfolio mixes. Some countries use subsidies delivered through the taxation system as a prominent means of encouraging private investment in affordable housing. Debate about Australia’s tax system has been underway since the early 1980s, culminating in the last few years in a major program of reform.

The introduction of the New Tax System, including the GST, in July 2000 has implications for housing investment. Investment in rental dwellings is input taxed under the GST, which means that although rents are exempt, input credits cannot be claimed by most investors on construction, maintenance, management and renovation of the asset and GST is payable on the sale of new and substantially renovated homes. However, charitable social housing providers registered for the GST can claim input credits. This may offer some scope for joint ventures between charitable providers and private investors utilising the GST status of the former.

A fuller treatment of taxation issues in the context of this study is put off until stage 2 of the project. Recommendations of the second stage of the Ralph Report on business taxation reform will be publicly released on 7 December. Preliminary advice to the researchers from Clayton Utz recommends waiting until this information is available before seeking detailed advice on the implications of recent changes in taxation regimes for investment in affordable housing.
The Growth of Superannuation Savings.

One of the major developments in the Australian capital market over the past decade and a half has been the extension of minimum superannuation coverage to virtually all workers. The total volume of superannuation savings in Australia stood at about $450 billion (Monash Sustainability Enterprises, 2000, p. 8) in early 2000. This figure is expected to reach $2 trillion by 2010 (Clark et al., 1996). This, in short, is where ‘the weight of money is.’ If private investment is to flow into affordable housing then the superannuation funds will be major players.

In a definitive study of the rise and role of superannuation or pension funds in the Anglo-Democracies, including Australia, Gordon Clark (2000) argues that ‘alternative investment products’ or AIPs, incorporating what have earlier been referred to as economically targeted investments and socially responsible investing, potentially provide a rapidly growing source of funds for socially important purposes, like urban infrastructure, venture capital and housing. Most AIPs have, as Clark stresses, been delivered in one-off packages, entailing very high transaction costs. Because they are one-off, trustees face problems of ‘veracity’, how to gain sufficient independent and reliable information on which to judge the real – as opposed to claimed – characteristics of the product on offer. What is required, Clark argues, is the intervention of second order financial intermediaries to reduce the ‘opacity’ of investment products like AIPs, to share or allocate risks among the various interests involved and to guarantee a degree of liquidity or an ‘exit option’ for pension funds wishing to sell their stake. Clark identifies a number of forms that such intermediaries could assume. One form is to develop new specific purpose mutual funds with a defined investment charter. Thus, in the United States the AFL-CIO Housing and Building Investment Trusts have been established to direct the savings of workers into construction projects throughout the country. HITs and BITs, as they are known, rely on a government mortgage guarantee as part of their risk allocation structure.

In Australia in the mid-1990s, the (then) National Mutual insurance company teamed with a number of ACTU industry superannuation funds to establish the Superannuation Members Home Loans Scheme as a vehicle for those funds to advance mortgage loans for home purchase to their members at highly competitive rates. This vehicle is owned by National Mutual/AXA and issues mortgaged backed securities by pooling the loans of individual fund members and selling the securities back to the funds.

Clark argues that AIPs delivered in the forms just described tend to depend on existing financial products. He also points to more innovative organisational forms of intermediation that manage very large volumes of funds allowing new AIPs to be developed, say with a focus on housing, on the margins of highly diversified portfolios. This effectively reduces the design costs of the new products by trading on the ‘sunk costs’ of the established organisation. Such organisations are able to hold the AIPs for the longer term, in line with the liability profiles of investing funds, unlike smaller less diversified organisations (Clark, 2000, p.197).

4 Investment Patterns in Rental Housing

The key question is – to what extent is the private rental sector able to meet the challenge of falling affordability? This question turns on the nature of investment patterns and incentives in this sector. This report first summarises the key features of current rental investment patterns, based on a survey of individual landlord-investors carried out in the late 1990s by the Australian Bureau of Statistics. This survey described an industry in which most of the rental stock was owned by small landlords holding one, sometimes two, properties for rent. The motivations for investing in the sector were diverse. Most investors were concerned about achieving long term, secure gains. Many seemed relatively unconcerned about maximising investment returns in the conventional sense. Indeed, perhaps as many as 30 per cent of this group could be described as ‘accidental landlords’. Actual reported returns to investors also varied widely. Gross rental
yields ranged from less than 5 per cent (8.3% of investors) to more than 8 per cent (29.3% of investors). Net returns before tax were negative for 35.9 per cent and positive for 29.4 per cent of investors. Higher income investors tended to be more represented among those receiving low yields and negative net returns, than low income investors, perhaps reflecting the former group's greater interest in negative gearing and capital gains.

What is clear, however, is that the private rental sector in Australia is a ‘cottage industry’ – ie it is dominated by small, non-professional investors. Large, institutional investors are absent from this sector, which is not the case in a number of overseas countries (see below). However, Commonwealth and State governments have over the past fifteen years evinced interest in attracting these investors into the provision of affordable, especially rental housing, for the following reasons:

- The increasing ‘welfarisation’ of public housing has resulted in a switch of government funding away from adding to the public housing stock towards rent rebates for low income public tenants. Funds have also been diverted from additions to maintenance and renovation of the existing stock.
- Government constraints on public borrowing has also limited the capacity of governments to meet the growing demand for affordable housing described above.
- Financial deregulation has opened up opportunities for new investment products.
- The general political climate has favoured a move towards ‘smaller government’ and greater involvement of the private sector in areas that once were the preserve of government.

During the 1980s and through the 1990s a number of new developments involving public-private partnerships targeting institutional involvement in the housing sector emerged, often short-lived. They included:

- **Debt securitisations.** A secondary mortgage market was initiated by State government borrowing schemes to finance low income home ownership in the late 1980s. Most of these schemes were capped or phased down during the 1990s. However, in the latter half of this decade a robust secondary market did develop and is growing rapidly, driven by the major institutions, including the expanding superannuation sector. Mortgage backed securities are now widely traded and include cross-border floats (Eurobonds).

- **Rental Housing Trusts.** Changes in Federal tax laws in the mid-1980s encouraged an initial flurry of interest in tax-effective rental housing trusts, driven by tax relief on nominal capital gains and a generous building allowance. However, a subsequent reduction of the building allowance and tight income taxation rulings concerning government guarantees to investors effectively closed off this approach.

- **Joint ventures.** A number of States developed partnerships, usually one-off, with developers or investors to provide housing, utilising headleases or sale-and-leaseback arrangements. Taxation rulings and Loan Council constraints limited developments in this direction, leaving joint ventures with equity investors as a possibility. Schemes like the PEP 1 and PEP 2 between the NSW Housing Department and AMP were introduced or, at least, considered. Developments to date have been limited and experimental. A number of the States are currently seeding new partnership arrangements with private sector and non-profit organisations.

- **Town planning controls.** A number of planning mechanisms are being used, particularly at local government level, to encourage the provision of affordable housing, often within a mixed income framework. Mechanisms drawn upon include: density or floor level bonuses; transferable development rights; flexible development standards, inclusionary zoning and linkage fees or levies. Often this approach will require new State legislation or amendment to existing legislation to allow responsible planning authorities to impose the controls on
developers. A recent example is offered by the Green Square residential development in inner South Sydney which involved developer and state government legal challenges to inclusionary zoning requirements for affordable housing and required two legislative amendments to enforce.

- **Ethical investment.** Ethical investors invest with a view to achieving a number of goals besides or in addition to commercial returns. They may be willing to accept less than the normal risk adjusted rates of return – in other words, to trade off part of these returns for other desirable goals, like employment generation or environmental enhancement. More frequently, they will be interested in what have been called ‘economically targeted investments’ or ETIs, which deliver normal market returns in addition to other collateral benefits. This is the form that ‘socially responsible investment’ (SRI) is assuming in Europe and North America. SRI is beginning to make inroads in Australia’s capital market with environmentally screened investment products offered through Westpac bank and about to be launched by IOOF. Ecumenical Housing Inc. has developed two affordable housing models based on accessing ethical investment. This field is likely to grow in Australia, offering funding opportunities for affordable housing.

**International Experience in the Private Funding of Affordable Housing**

Private investors, including the major institutions, are heavily involved in funding affordable housing in a number of European countries and North America.

In the *United States*, Federal government initiated agencies, notably Fannie Mae, dominate the secondary mortgage market. Fannie Mae facilitates about one-seventh or all residential mortgages in the U.S. through the issue of mortgage backed securities, most of which are purchased by pension and mutual funds. Non-profit organisations and partnerships between government agencies, non-profits and private investors proliferate at the local level to facilitate low cost access to home ownership.

The major policy tool for encouraging private investment in rental housing has come through Federal Government housing vouchers and taxation relief. The ‘section 8’ scheme delivered subsidised rents to investors willing to lock up their properties in low income usage for 20 years. The scheme was phased down from the early 1980s. The *Low Income Housing Tax Credit* Program was introduced in 1986 and provides tax credits (sometimes topped up by state government income tax credits) to developers providing rental units to low income tenants for a period of at least 30 years (with an escape clause at 15). About 900,000 dwellings have been provided under this program, renting at an average of 9 per cent below the national average rent.

A number of U.S. cities, like San Francisco and Boston, operate inclusionary zoning and linkage policies that require developers to include some affordable housing in their residential and commercial developments (or make equivalent payments to the city government in lieu).

In the *United Kingdom*, as in most Western European countries, government policy has emphasised the role of the housing associations. The local government public housing sector remains large but has fallen from about a third to a little over a fifth of the total housing stock since 1980. Housing association additions are funded by a mix of central government grants and private loan finance. Housing allowances are paid to low income tenants. Recent attempts to encourage institutional equity investment in rental housing through tax relief – the Business Expansion Scheme and Housing Investment Trusts – have not been successful. However, recent research has identified increasing institutional interest and some involvement in providing rental housing.

*The Netherlands* has a large and diverse housing association sector, accounting for about a third of the national stock. This sector has been built up over time supported by a range of
direct government subsidies, on construction and operation. However, in the 1990s policy changed and direct subsidies were phased out in favour of an one-off capital grant that transferred ownership of the existing stock to the associations. This provides a solid equity base for the associations to borrow from the institutions to expand and maintain the stock. Private investment in the sector is supported by a triple-system of guarantees or insurance. First, housing associations must satisfy minimum capital asset requirements in order to demonstrate their solvency. Second, loans to individual associations are guaranteed by a central fund established by an initial government grant and continuing contributions by all associations. A second central fund has been set up by association contributions to provide financial assistance to and reorganise individual associations which get into financial difficulties. Third, local and central government provide a final line of insurance, and are expected to participate with the second central fund just noted in assisting associations in financial difficulty. As a result of this support structure, housing associations in the Netherlands are able to borrow from the institutions at a rate very close to the government bond rate.

Past Australian Studies of Private Sector Involvement: Confronting the Barriers

The report summarises the findings of a number of past studies into the possibility of private investment in rental and affordable housing. In spite of the range of approaches covered and issues canvassed, an overall conclusion of these studies is that current conditions in Australia have not, to date, facilitated private sector investment in this sector. A number of significant barriers exist preventing more interest, especially by the institutions, in the provision of rental housing at the affordable end.

The report details the following barriers preventing more activity in this sector:

- Low returns
- High risks – revenue, credit, financial and political risks
- High management costs
- Illiquidity
- Poor and incomplete market information on the performance of housing as an asset
- No established track record for this asset class

Dealing with the issue of inadequate returns, given the perceived risks, is central to encouraging greater private investment in the sector. The report outlines two main ways of closing what is termed the affordability rent gap – the difference between the rent level necessary to meet the required rate of return by investors and the (lower) ruling market rent.

The first way entails bridging the gap through providing government subsidies of one form or another: cash, tax relief, cheap land or via town planning controls. The second way involves reducing the rent required by:

- Increasing operational and/or financial efficiencies – ie reducing investor costs associated with housing provision
- Reducing risks or transferring risks to other parties by means of insurance, guarantees and/or the provision of better quality market information which allows investors to more finely price risk.
- Enhancing the importance of capital gains relative to rental yield in overall investor returns.
- Government prescription – eg by imposing direct regulatory control over the asset allocation investment decisions of investors.
Introduction

The Australian housing system has, historically, been dominated by a concern for creating and maintaining a large and diverse population of home owners. Renting has generally been viewed – by policy makers, investors and public at large – as a residual or temporary tenure. Owner occupation was held up as the ‘normal’ state of residence for Australians, and as a vehicle for achieving a range of positive social and economic goals (Stretton, 1970; Kemeny, 1983; Neutze and Kendig, 1991; Troy, 1991).

Australian housing policy in the Post-War period has been divided between facilitating access to home ownership through a combination of regulatory and subsidy arrangements (eg. interest rate caps, mortgage insurance provision, home savings grant and tax relief) and provision of what, by OECD standards, is a minimalist social housing sector (Dalton, 1999; Yates, 1989, 1997). Issues of housing affordability have, therefore, been caste within a dual discourse – one strand concerned with issues of interest rate levels, deposit gaps, land development and construction costs, and the like, the other strand focused on targeting public housing to households deemed to be most in need and most at risk of poor housing standards, or worse, homelessness. The underlying assumption for most of this period, however, was that a combination of continuing economic growth and benign government policy would ensure affordable and appropriate housing standards for the vast majority of the population.

Developments during the 1990s have placed a large question mark against this general assumption (Berry, 1999; Badcock and Beer, 2000). Housing affordability – or the lack thereof – emerged during this decade as a major problem and focus for housing policy reform. Paradoxically, during a long boom of sustained economic growth and historically low (nominal, if not real) mortgage interest rates more Australians than ever were struggling to adequately house themselves.

The signs of increasing housing stress include: a declining first home owners market, a slowdown in additions to the public housing stock, continuing loss of low cost rental dwellings, and rising numbers of low income households required to pay in excess of 30 per cent of their incomes in rent or mortgage repayments. Recent research also suggests that the private rental market is playing an increasingly important role in the overall housing system. Renting has become a permanent housing tenure for a significant and (probably) growing proportion of the population. Wulff and Maher (1998) found that 40 per cent of private tenants had been renting for the previous 10 years or longer. Berry et al (1999) discovered signs of an increasing incidence of mortgage default during the 1990s – ie. of people ‘falling out of home ownership’ – albeit from a low base, and therefore dependent on rental housing of one kind or another. Most ominously, homelessness has reappeared as a serious social problem and policy concern. The most authoritative estimate of incidence, based on a detailed analysis of the 1996 Census, found that on Census night ’96, more than 100,000 Australians were, technically, homeless, including more than 20,000 suffering ‘primary homelessness’ (literally without a roof over their heads) (Chamberlain, 1999).

Recent research by Yates and Wulff (2000) has found that although the rental market grew substantially in the 1986-1996 period – much faster than owner occupation and the number of households – this growth was highly uneven across rental segments or sub-markets. In particular, the stock of low-rent dwellings actually fell over this period by 28 per cent, an absolute stock decline of almost 70,000 dwellings, while the stock of moderate and high-rent dwellings rose by over 70 per cent. Over the same period, the number of low and moderate income households grew strongly, also at rates in excess of 70 per cent.

What this study points to is an intensifying mis-match between the number of households requiring low-cost rental housing and the availability of a dwindling stock of low-cost rental dwellings. In particular – using the conventional affordability benchmark of 30 per cent – Yates
and Wulff estimated the shortfall of low cost rental stock at almost 50,000 dwellings in 1996, Australia wide. Higher income households, on the contrary, faced a situation of greater and growing housing choice.

In short, during the 1986-1996 period, the rental market in Australia polarised on income grounds, narrowing the opportunities for low income households to secure affordable housing, while enhancing the effective housing choices of higher income groups.

What this analysis underscores is that the housing system is characterised by significant forms of market failure. Chronic and increasing excess demand/supply shortages persist in the low cost rental sub-market. Contrary to conventional economic theory, excess demand in this segment does not automatically bring forth a corrective supply response. Private investors have not rushed to fill the gap, investment has not flowed into addressing the developing shortages.

Yates and Wulff go on to argue that the real situation is even worse than the aggregate analysis suggests. In 1996 only 42 per cent of low cost rental dwellings were occupied by low income households. The remainder – in excess of 100,000 dwellings – were occupied by higher income households paying relatively low proportions of their incomes in rent. A similar pattern of ‘crowding out’ characterised the low-moderate income segment. Hence, to the extent that there is ‘over-consumption’ of housing in Australia, it is concentrated in relatively affluent sub-markets. Moreover, over-consumption in these segments directly contributes to significant and growing under-provision of affordable housing to low income households; both outcomes are opposite sides of the same coin, expressions of permanent inefficiencies in housing markets overall. Allowing for this fact, Yates and Wulff re-estimate the national shortage of low cost rental dwellings in the mid-1990s at around 150,000. The analysis presented in chapters 2 and 3, below, strongly suggests that the situation worsened in the latter half of the 1990s – and is likely to continue to do so, unless appropriate government policies are implemented.

Space or location provides a further dimension to the mis-match problem. Shortages of low cost rental dwellings are more intense in some regions and sub-regions than others. The ready availability of affordable housing in some areas (i.e. local surpluses) does not automatically solve shortage problems elsewhere. For example, vacant low rent houses available in the Latrobe Valley do not significantly ease Melbourne’s affordability problems. Melburnians unable to find affordable accommodation do not necessarily move to the Valley, in part because low rents and excess stock there also reflect poor local employment opportunities. The operation and inflexibilities of regional labour markets reinforce the spatial mis-match of housing needs and opportunities. This fact suggests that the national estimate of a 150,000 shortage in low cost stock is likely to be a substantial under-estimate of the true scale of the problem. Too many low-rental dwellings are in the wrong place! The crucial significance of geographical or locational differences in gaining an accurate picture of current housing problems is addressed in chapters 1 and 2 of this report.

Pervasive rental market failure in Australia is creating increasing problems of affordability and associated hardship for low and low-moderate income households. As the detailed data presented in subsequent chapters demonstrates, housing stress is intensifying, most notably in our metropolitan centres. Inadequate housing has far-reaching economic and social costs, both for the households directly concerned and the community at large. These negative impacts and externalities can be summarised as follows.

**Direct Costs to Individuals and Families**

- **Housing related financial hardship.** From the time of the Henderson Poverty Inquiry in the 1970s, Australian research has consistently found a positive relationship between poverty and housing costs, especially for households in the private rental sector. The 30 per cent
affordability benchmark has been widely used to indicate the point beyond which a household is likely to suffer severe financial difficulties in meeting the necessary expenses of life other than housing -- e.g., food, clothing, heating, transport, education, health, etc. Where a household has insufficient resources to meet the barest of necessities, full participation in the normal life of the community is impossible and other problems multiply. In particular, some households are forced into situations of overcrowding which can transform into outright homelessness.

**Key Fact:** The proportion of Sydney’s low income private tenants paying more than 30 per cent of income in rent increased from 70 to 75 per cent between 1991 and 1996 (Hall, 1998).

**Overcrowding and homelessness.** These extreme problems often result when housing costs become prohibitive, which in turn exacerbates the range of problems discussed below. The definitive study of the size of the homelessness problem in Australia was released by the Australian Bureau of Statistics in early December 1999 (Chamberlain, 1999). This analysis treats as homeless people who are (1) without conventional shelter (i.e. sleeping outside, in railway carriages, etc), (2) accommodated in temporary shelters, refuges, night shelters, etc), including women and children escaping domestic violence and (3) living in boarding houses on a medium term basis but without access to a separate bedroom, kitchen and bathroom.

**Key Fact:** On Census night, 1996, 105,304 people were homeless, with more than 20,000 being without conventional shelter of any kind however inadequate (Chamberlain, 1999).

**Family instability and breakdown.** Inadequate housing and related financial stress can contribute to family breakdown, as well as resulting from it. This reciprocal effect is most apparent in the case of women forced to move to refuges. McCaughey (1992) has documented how, in such cases, normal family and parenting relationships are threatened and difficult to re-establish. Without secure tenure over housing of a reasonable basic standard, large enough to meet the minimum requirements for shelter of a household, given its size and composition, normal “family life” is extremely difficult to support.

A high separation and divorce rate imposes financial and psychological costs on family members, especially children, while increasing the publicly borne costs of the justice system. Divorce and separation are due to a complex set of factors and improved housing situation by itself is unlikely to reverse the trend. However, an increase in the supply, quality and targeting of affordable housing is likely to be part of the answer to more stable family relationships and overall improvements in the quality of family life.

**Lower effective access to the labour market.** Housing prices in a capitalist economy rise to reflect relative accessibility to, among other things, employment opportunities. The geographic concentration of lower cost housing in areas of low employment can markedly reduce the job prospects of households forced by lack of resources to live there. Poor job prospects reduce lifetime earnings and the capacity to meet long term housing costs. Van Kempen and Priemus (1999, p.648) also argue that the “(s)patial concentration of
unemployed people may hamper contacts with those who have a job. In this way, no information is exchanged on job openings’. In areas of high unemployment the informal social networks of friends, neighbours and local businesses, that might mobilise and communicate information about job opportunities are non-existent. Social isolation and stigma attached to such enclaves reinforce the disadvantages of unemployment, including real and perceived discrimination by employers.

**Key Fact:** In a study of a public housing estate on Sydney’s South-Western fringe, Stubbs (1996, 1998) found that the unemployment rate on the estate was four times that for NSW, as a whole. The cost to the community was estimated at $46,000 per unemployed tenant, when the direct cost of government benefits and labour market programs was added to the indirect costs of administration, support services and loss of potential contribution to GDP.

- **Health problems.** There is a large body of evidence linking poor housing situation to a range of serious health problems for household members.

  The National Health Strategy (1992) found a strong link between low economic status and poor health. In the absence of adequate and affordable housing, homelessness and overcrowding can pose serious health dangers. Herrman (1991) found that almost half the homeless people interviewed had experienced a severe mental health disorder in the preceding month, though clearly the causes are complex and interacting. Cass (1991) identified evidence of poor nutrition, especially of children, when people did not have access to basic cooking facilities. Clough (1991) found that among homeless people, the prevalence of illness included respiratory problems (especially among those "sleeping out"), dental problems and a susceptibility to a range of infectious diseases. Problems of substance abuse are also high among the homeless (Burke, Hancock, and Newton, 1984).

  **Key Fact:** low socio-economic status residents in public housing in Adelaide have better health outcomes than similar households in the private rental market (Geddes, 1993).

The inter-linked problems of poor health and inadequate housing are extreme for Indigenous Australians. Aboriginal households are concentrated in public and private rental housing. They have low average incomes and suffer high unemployment. During the 1990s, the unemployment rate among Aborigines has remained above 40 per cent. Major reports by Jones (1993) and Pholeros (1993) have detailed the often appalling housing and health problems faced by Indigenous peoples. Pholeros’s study found significant reductions in rates of infection for a range of illnesses when basic improvements were made in water, sewerage and other domestic hygiene facilities.

Other marginalised groups with special housing needs can also be disadvantaged. For example, people with HIV/AIDS can face difficulties in gaining affordable housing located near appropriate health facilities, their health plight often reinforced by discrimination. In general, where a lack of affordable housing options force households into poor quality or
overcrowded conditions, or push them out to marginal, isolated areas, health problems are likely to multiply.

- **Crime.** The links between crime and inadequate housing are complex. Clearly, a range of factors, including poor housing, are responsible for current crime levels and outcomes. In a British study, Barrow and Bachan (1997) compared crime levels and costs across London public housing estates. They found that, for example, the annual costs of dealing with crime in the deteriorated and stigmatised London estate of Stepney was more than four times the level for the newer and better resourced Paddington estate. In Australia, anecdotal evidence points to a link between illicit drug dealing and substance abuse concentrated on large public housing estates. This creates obvious problems for estate residents and imposes significant costs on state housing authorities, in the form of higher management costs and vacancy rates. Providing housing that is both appropriate and affordable is one of a number of strategies necessary for dealing with the problems criminal activity impose on victims and the broader community.

- **Low levels of educational attainment.** Children living in temporary, overcrowded or otherwise inadequate housing may suffer educational disadvantage. Poor housing leading to poor health can, in turn, adversely affect school attendance and performance. Insecurity of tenure and frequent forced moves can disrupt a child's schooling and encourage truancy. Overcrowding and frequent relocation may reduce the ability of children to complete homework and other out-of-school tasks. Poor educational performance imposes lifetime costs on the individual, in terms of confined employment opportunities and income foregone, and on the broader society which does not benefit from a well educated and trained citizenry.

**Costs borne by the Community**

In an increasingly polarised world the social links and networks which help to create a cohesive, productive society weaken. The capacity of local communities to mobilise and deploy social capital is reduced. Social capital "...refers to the norms and networks of civil society that lubricate cooperative action among both citizens and their institutions. Without adequate supplies of social capital -- that is without civic engagement, healthy community organisation, norms of mutual reciprocity and trust -- social institutions falter" (Putnam, 1998, p. v).

In a special issue of the U.S. journal, *Housing Policy Debate* (vol.9, no 1, 1998) a number of papers focused on the links between social capital formation and adequate housing. Permanent, secure housing, it is argued, provides the necessary base for social capital - mutual trust, cooperative behaviours, etc - to emerge and "get a grip." Saegert and Winkel's (1998) contribution found that, once established, social capital was critical in the success of a locally driven scheme for low cost housing which redeveloped derelict and deserted properties whose owners had defaulted on property taxes. In this case, housing quality was improved and the local crime rate fell. Temkin and Rohe's (1998) study of Pittsburgh found that neighbourhood stability in the sense of low resident turnover, was associated with both high levels of social capital and good, basic, housing standards. Stability, in turn, reinforced social networks and provided a secure residential environment in which people could securely plan their overall lives.

Where social cohesion breaks down on a broader metropolitan-wide scale or between city and country, perverse signals lead to an increase in defensive expenditures. People living in affluent areas spend heavily on personal and dwelling security systems. The phenomenon of the "gated estate", prevalent in some U.S. cities, is a collective example of particular communities "throwing up the shutters". Once begun, the process of withdrawal and self-defence is self-reinforcing. As crime rates and insurance premiums rise, the bonds of community -- social capital across space -- atrophy. Cities become dangerous - and at times and in certain places --
deserted. Moreover, defensive and excessive expenditures on housing by more affluent households are essentially unproductive from the viewpoint of the economy at large. Resources that could be flowing into financing innovation and new businesses are locked within the housing system as privileged sub-groups seek to protect themselves from the loss of community that, collectively, their very actions are encouraging. These social costs of community division can have adverse economic consequences for global cities like Sydney. The social environment, especially the perceived safety and health of a city, are important magnets for investment and the location of managerial staff and knowledge workers in the dynamic growth industries. Tourism depends critically on the image and substance of a city or region’s social (as well as physical) environment. Innovation, continuous productivity growth and competitive advantage require well-structured and functioning city systems. This is important as a basis for firms to minimise their costs while maximising the synergies of co-location in large, integrated labour and product markets. At one level this means adequate investments in modern, reliable and timely infrastructure in transport, health, housing and education. At another and increasingly important level it means the development of informal contacts and information exchange — the so-called ‘soft infrastructure’ basis of business that draws the head office operations of global enterprises to locate in the CBDs of a handful of world cities. Around these corporate decision making centres gravitate or ‘cluster’ a plethora of specialist consulting organisations and intermediaries, facilitating communication within the corporate world and between it and government. Informal, face-to-face contact is still vital to the corporate elite and knowledge workers generally. It is they who are the ultimate resource in determining a region’s relative economic performance. Where they and their families choose to live is a matter of vital economic concern to Australia. These workers are increasingly in demand and mobile on a global scale. The creation and maintenance of a safe, cohesive and productive urban environment, free from the excesses of social division and conflict, is one critically important way to attract and keep these workers, and is therefore a prerequisite for successful competition in today’s world.

At a strictly functional level, too, global cities need plenty of lower paid service workers, as well as high flying knowledge workers. If routine office workers, cleaners, restaurant workers, shop sales persons, bus drivers and the like are unable to afford to live anywhere near the centres of economic activity, their lives are impoverished and the regional economy also suffers from inefficient workers or labour shortages. These problems are clearly evident in dynamic world cities and regions like London and Silicon Valley¹ — and may increasingly constrain innovation and growth in Australia’s major centres. Once begun, the process is cumulative. Marginalised households become trapped in areas of high unemployment and lack of economic opportunities, pushing out the remaining higher income, skilled and more mobile workers and entrepreneurs and entrenching the areas as locii of disadvantage and despair. The result is a self-reinforcing spiral of falling population, average incomes, employment and housing values. Poorly integrated urban transport systems weakly articulated with effective housing opportunities over the metropolitan region is a recipe for economic as well as social disaster in the era of the new knowledge economy.

A British study by Meen and Andrew (2000) highlights this cumulative process of decline in parts of inner-London and polarisation at the metropolitan scale. Knowledge workers and other high-income households have moved away from these areas to suburban or ex-urban locations in search of better housing conditions and environmental amenity, commuting back to the centre where necessary. Lower income and marginalised households remain trapped in the inner areas and tend to travel much shorter distances to available work. Since economic restructuring has impacted negatively in a significant way in those areas, resulting in large-scale job losses in traditional manufacturing and service industries, local unemployment rates have

¹ Escalating housing costs and stress is apparent in a number of high-tech regions, including London, Boston, Silicon Valley, San Francisco and Seattle (see: Greater London Council, 2000; Mayor’s State of the City Speech www.ci.sf.ca.us/moh/housing.htm; Silicon Valley Manufacturers Group (1999); Affordable Housing in Seattle and King County www.metrokc.gov/exec/commentary/022599com.htm).
risen, encouraging further flight by the remaining more mobile, higher income residents. Falling populations and incomes make it even more difficult for poorer households to move out, especially if, as in the South-East of England during the 1990s, they hold negative equity in their properties as home owners or face ever-increasing relative rents elsewhere in London as tenants.

Although London’s particular situation differs from the social and spatial patterns of Australian cities, the overall thrust of this research remains relevant. In both cases poorer households disadvantaged in the labour market suffer reduced effective access to affordable housing. This helps to lock or entrap people in areas where employment opportunities are shrinking, reinforcing their low income status and further confining their effective housing choices in a cycle of decline and deprivation. In this way, different parts of the city – and, more broadly, different regions – diverge from rather than converge towards similar patterns and levels of development. The exclusion and lack of mobility of the urban unemployed reduces the overall efficiency of the metropolitan and national economies, raising the prospect of labour shortages and bottlenecks alongside pronounced pockets of permanent unemployment.

This picture of the emergence of multiple and mutually reinforcing disadvantages, expressed ‘on the ground’ in the form of spatially segregated cities in which accumulated social capital is disappearing, raises the spectre of large scale social exclusion. Social exclusion refers to the disconnection of sections of the population from the mainstream social institutions of society – from jobs, family, communal organisations and the like – with little likelihood of re-connection. Whereas polarisation is primarily focused on distributional concerns, social exclusion is concerned with relational issues – i.e. with the notion that some people are effectively being prevented from full participation in the life of the community. There is a lack of social integration in society that leaves the marginalised powerless to exert their full rights of citizenship in the sense first enunciated by T. H. Marshall in the early 1950s.

The weight of evidence is clear. Adequate and therefore affordable housing is a necessary means to achieving and maintaining an inclusionary, innovative and productive society. Deep and pervasive market failure in Australian housing markets – as earlier described – means that current housing policies are inadequate and inimical to Australia’s long term welfare. The ‘do-nothing’ option in the face of rising housing affordability problems is a threat to future living standards. There is a strong and growing case for new housing policy initiatives.

This report first establishes the scale and intensification of the affordability problem in Australia over the past 15 years and then analyses the existing barriers to adequate investment flows into the provision of affordable housing, in the current policy context. A framework for considering the range of potential avenues for greater private investment in affordable housing is presented. Each avenue has implications for appropriate public policy.

**Structure of Report**

Within this context, Chapter 1 of the report details recent trends in housing affordability in Australia, concentrating on developments in three major metropolitan regions, Sydney, Melbourne and Adelaide. Data on movements in rents, dwelling prices, interest rates, cost of living and household incomes are compared between these cities, over the 1986 to 2000 period to identify the main trends relevant to the question – how affordable is housing of different types in different locations for different sub-groups? These cities have been selected because they offer a range of underlying factors impinging on affordability and, importantly for our purposes, have consistent and comparable data for the period chosen for analysis. In the case of Brisbane, Perth and Hobart it was not possible to extract relevant data in a suitable form over the period chosen. For example, the Queensland Valuer General does not release data for the metropolitan region on property sale values, as in the other states. Similarly, private rental data equivalent in scope and quality to that available in other states is not available for Perth. Rent and price data on the capital cities produced by the various state real estate institutes are not
complete nor do they cover the period chosen for analysis. In order to discern clear trends it is necessary to cast the analysis over a suitably long period, in this case from 1986 to 2000. In order to make meaningful comparative statements about affordability trends it is necessary to have data on household incomes, rents and mortgage payments that are consistent with relevant Census spatial categories (in this case ABS statistical regions and sub-regions and statistical districts and sub-districts).

Earlier studies of housing affordability have tended to concentrate at an aggregate level or on a single city (eg. Hall, 1999; Cardew, Parnell and Randolph, 2000) or are dated (eg NHS, 1991). This report brings the picture up to date at a sub-regional level of analysis, covering three major metropolitan regions.

The analysis in this report focuses on both (1) affluent (inner) areas and lower priced outer locations of selected cities and (11) three bedroom fully detached houses and small one bedroom units. Housing choice is defined by both what people can afford and by the suitability of the particular dwelling for their needs. Suitability relates to the type, size and the location of that dwelling. For example a one bedroom dwelling is simply inadequate for a family of four, and for this reason the ability to pay the required dwelling price, i.e. rent or mortgage is not sufficient in any analysis of affordability issues. Some dwelling types and locations will be completely inappropriate for many households and therefore we have examined affordability across two dimensions, the range of possible dwelling types, and the range of possible prices by locations. This enables a more accurate picture to be drawn of emerging affordability trends than would be the case if the analysis was cast at the metropolitan or state-wide scales.

**Key Findings**

Over the 1986-1996 period:

- Real median household incomes fell by 13% in Adelaide, 11% in Melbourne and 4% in Sydney. The fall was worse for lower income householders. The lowest 40% of income earners experienced declines of 16%, 12% and 5% in the three cities, respectively. This trend is consistent with the emergence of ‘the working poor’, employed people who increasingly do not meet the lending criteria of financial institutions and are effectively excluded from home ownership.

- Rents and prices of fully detached houses have grown faster than the household incomes of the bottom two income quintiles, throughout the three metropolitan regions (with the exception of rents in outer Melbourne). House prices and rents have risen strongly across these cities in the latter half of the 1990s.

- Rents and prices of small multi-dwelling units also rose ahead of incomes in the inner areas of the three cities for the bottom two income quintiles. The opposite was the case in outer Adelaide and Melbourne. However, in Sydney, even this narrow relief from declining affordability did not eventuate; rents and prices across the dwelling types everywhere rose faster than incomes for this group.

Chapter 2 focuses on the implications of changes in affordability for levels of housing stress. Changes in the proportions of tenants paying more than 30 per cent of their household incomes in mortgage repayments and rents are traced in the three cities concerned. The evidence clearly points to private renting as the locus of severe housing stress in Australia. It is in this sector that the supply response of the market appears least robust, and the need to stimulate more private investment most pressing. Extending the analysis to other tenures would, to some extent, dissipate or hide the current serious extent of housing affordability problems in the rental sector. The report focuses on private tenants because the earlier NHS and other research found very low proportions of outright home owners and public tenants to be paying in excess of 30
per cent of their incomes for housing, as well as the difficulties involved in interpreting the discretionary or choice element in the case of purchasing home owners. The most recent housing survey carried out by the Australian Bureau of Statistics (1999) found that the proportion of outright home owners paying more than 30 per cent in housing costs was 4.9 per cent. The figures for purchasing owners, public tenants and private tenants were 27.9 per cent, 9.9 per cent and 54.7 per cent, respectively. Changes in Australia’s financial sector during the last 15 years have resulted in large and increasing flows of savings into financing home ownership. The rapid recent growth in the secondary market for residential mortgages underscores the relative neglect of the private rental sector, especially by large corporate investors. Capital constraints on both public borrowing for public housing and investment in private rental housing is contributing to the worsening affordability problems being experienced in the private rental sector. Consequently, the need for innovative policy interventions is likely to be most needed in this sector and this forms the focus for this report. Unless appropriate policies are implemented to overcome the problem of an inadequate supply of rental housing, by encouraging greater private investment, the already severe problems of affordability detailed in chapters 1 and 2 of this report are likely to worsen.

Key Findings

In June 2000 it is estimated that no low income rental household could:

- Afford to buy a three bedroom house anywhere in Melbourne, Sydney or Adelaide.
- Afford to buy a one bedroom unit anywhere in Sydney, with only 15 per cent of Melbourne households being able to buy in the outer area (but not inner area).
- Afford to rent a three bedroom house anywhere in Adelaide. Only 9 per cent of households in Melbourne and 3 per cent in Sydney could afford to rent this dwelling in the outer areas (but not inner areas).
- Only very small proportions of low income tenants are able to afford to rent a one bedroom unit in inner Melbourne or inner Sydney (less than 5 per cent). Conversely, more than 50 per cent of these households could afford to rent this dwelling in the outer areas of the three cities.

Between 1986 and 1996, the proportion of low income tenants in housing stress – i.e. paying more than 30 per cent of their incomes in rent – rose from:

- 63.4% to 76.1% in Adelaide
- 60.5% to 74% in Melbourne
- 67.3% to 80.7% in Sydney.
- Brisbane from 63.7% to 64.3%;
- Perth from 59.9% to 56.1%;
- Hobart from 57.7% to 62.4%;
- Darwin from 70.7% to 63.7%; and
- the average for all capital cities from 64.1% to 72.7%
Chapter 3 addresses the changing public policy environment in Australia. The changing emphases and directions in housing policy are first identified, particularly the withdrawal of government from aggressive attempts to increase home ownership and the relative switch of emphasis in housing assistance from public housing to rent assistance. The important and ongoing issue of taxation reform is then raised. Finally, the significant growth of the superannuation sector is outlined, with implications for a rising demand for new domestic investment products.

The final chapter focuses on the patterns and forces driving investment patterns in housing, particularly rental housing in Australia. To what extent are existing flows of finance into the housing sector contributing to the patterns of housing affordability and stress identified? Where are the gaps in provision? The limited role (currently) of institutional investors is analysed. The report summarises a number of attempts in Australia to attract private, including institutional investment into the provision of affordable housing over the past two decades. These approaches tend to fall into a number of categories; debt securitisation, rental housing trusts, joint ventures, town planning controls and ethical investment. By comparison to other countries, Australian developments in this area have been small scale, fragmented and relatively unsuccessful. The report therefore briefly and selectively describes attempts in a number of other countries – notably, the United States, Britain and the Netherlands – to encourage greater private sector investment in affordable housing, further illuminating the key factors and constraints at work. The report then summarises the main conclusions of a series of Australian studies that have been carried out over the past ten years or so which have looked at different approaches to attracting investment into this sector. The chapter concludes by providing a framework for considering the key issues and constraints identified by these studies and both overseas and local developments designed to boost private investment in affordable housing.

- The total increase in the number of low income households in housing stress for the seven capital cities was 90,000 between 1986 and 1996 (the increase for all tenants paying more than 30% of income in rent was 116,750 over the same period).
- In 1996 in the capital cities of Australia some **227,480 households** within **bottom two income quintiles** were experiencing housing related stress.
- The provision of new physical dwellings to directly meet this shortfall would cost in the order of $27 billion.
- The current **Rent Assistance** program has not reversed the trend of declining housing affordability.

In summary:
- In the capital cities of Australia nearly 3 out of every 4 private renter households (with incomes in the lowest two income quintiles) are now experiencing housing stress.
- For five out of the six capital cities and Darwin, stressed households are growing more rapidly than total renter households in the same income categories.
- **If the rate of growth of stressed households experienced in the last 10 years continues, then the number of households experiencing stress will double in fifteen years and reach nearly one million within 20 years.** Furthermore this analysis understates the problem because it ignores the
## Glossary

Comprehensive statistical analysis has been completed on 7 statistical subdivisions in the capital cities of Adelaide, Melbourne and Sydney. These were chosen after examining the dwelling price and rent characteristics applying and contain the highest and lowest priced markets. The subdivisions and the Local Government Areas within them are listed below.

### Northern Adelaide
- Gawler (M)
- Playford (C)
- Port Adel. Enfield (C)
- Salisbury (C)
- Tea Tree Gully

### Eastern Adelaide
- Adelaide (C)
- Adelaide Hills
- Burnside
- Campbelltown
- Norw. P'ham St Ptrs (C)
- Prospect (C)
- Unley (C)
- Walkerville (M)

### Inner Melbourne
- Melbourne
- Port Phillip (C)
- Stonnington (C)
- Yarra (C)

### South Eastern Melbourne
- Cardinia (S)
- Casey (C)
- Gr. Dandenong (C)

### Inner Sydney
- Botany (M)
- Leichhardt (M)
- Marrickville (M)
- South Sydney (C)
- Sydney City (C)

### Eastern Suburbs
- Randwick (C)
- Waverley (C)
- Woollahra (C)
Outer Western Sydney

Blue Mountains (C)
Hawkesbury (C)
Penrith (C)
1 Trends In Housing Affordability Indicators

There are a number of indicators that collectively contribute to housing affordability. These are:

i. inflation, interest rates and real interest rates, (repayments required);
ii. incomes and earnings, (capacity to pay);
iii. unemployment and employment conditions; (market participation);
iv. dwelling prices and rents, (payment requirements);
v. mortgage and rent payments, (savings capacity, ability to increase housing consumption);
vi. tenure, (impact of market economics, housing choice); and
vii. mobility or frequency of residential relocation; (aggregate housing demand and price and rent impacts).

1.1 Inflation, Home Loan Rates and Real Home Loan Rates

Graph 1 sets out the Consumer Price Index, (CPI), standard bank home loan rates and real bank home loan interest rates over the period June 1986 to June 2000.

GRAPH 1

ADELAIDE, MELBOURNE AND SYDNEY; WEIGHTED AVERAGE CPI FOR SIX CAPITAL CITIES, BANK HOME LOAN RATES AND REAL HOME LOAN INTEREST RATES: June 1986 - June 2000

Australian Bureau of Statistics: Catalogue No 0401.0 Weighted Average Consumer Price Percentage Change

Bank home loan rates are at almost their lowest level for the last sixteen years having only been 1.1% lower at June 1998. Every 1% increase in mortgage rates equates with an almost 6% increase in mortgage repayments, however of more relevance here is the trend in real home loan mortgage rates. Real home loan mortgage rates are of more concern to the average home-owner in that it is assumed that most household incomes keep pace with inflation, (this assumption will be examined in a later sub-section). Therefore increases only in nominal rates, (but not real rates), and hence mortgage payments, will, with some timing differences, be matched by proportionate increases in incomes. On the other hand if real rates increase
mortgage payers are unlikely to have received compensating income growth with a commensurate increase in mortgage payment burdens.

Further examination of Graph1 reveals that real bank home loan rates at 4.47% have reached their second lowest level of the last sixteen years only being bettered by 4.34% that applied in June 1987.

1.2 Household Incomes and Average Weekly Earnings

Table 1 sets out Median Household Incomes and the threshold income for the lowest two household income quintiles for Adelaide, Melbourne and Sydney for the period 1986-1996 and Average Weekly Ordinary Time Earnings (AWE) for each State for the period 1986 to 2000. AWE refers to the individual weekly gross income of full-time workers.

Table1: Household Incomes and Average Weekly Earnings (Annualised), Capital Cities and South Australia Victoria and New South Wales: 1986 – 2000: $000’s

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Median Household Incomes</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Adelaide</td>
<td>21.25</td>
<td>27.71</td>
<td>29.88</td>
<td></td>
</tr>
<tr>
<td>Melbourne</td>
<td>25.37</td>
<td>32.68</td>
<td>36.32</td>
<td></td>
</tr>
<tr>
<td>Sydney</td>
<td>25.38</td>
<td>35.10</td>
<td>39.66</td>
<td></td>
</tr>
<tr>
<td><strong>Threshold Household Income: Bottom Two Income Quintiles</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Adelaide</td>
<td>17.31</td>
<td>22.24</td>
<td>23.74</td>
<td></td>
</tr>
<tr>
<td>Melbourne</td>
<td>20.59</td>
<td>26.43</td>
<td>29.34</td>
<td></td>
</tr>
<tr>
<td>Sydney</td>
<td>20.42</td>
<td>27.88</td>
<td>31.63</td>
<td></td>
</tr>
<tr>
<td><strong>Average Weekly Full Time Earnings: All Persons</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>South Australia</td>
<td>20.72</td>
<td>28.41</td>
<td>32.96</td>
<td>37.79</td>
</tr>
<tr>
<td>Victoria</td>
<td>21.17</td>
<td>29.33</td>
<td>34.66</td>
<td>39.83</td>
</tr>
<tr>
<td>New South Wales</td>
<td>21.46</td>
<td>29.50</td>
<td>36.59</td>
<td>42.75</td>
</tr>
</tbody>
</table>


Two aspects of Table 1 are worth commenting on, the first is the significant absolute difference in median household incomes between Adelaide households and the other two capital cities and the second is the rapid growth in average weekly ordinary times earnings (AWE), when compared to household incomes. Graphs 2, 3 and 4 examines household income growth and AWE versus inflation in each of the capital cities.
From these graphs it is clear that over the period 1986-1996 median household incomes and threshold household incomes for the lowest two household income quintiles have fallen considerably in real terms in all three capital cities. By contrast, particularly in the last four years, real AWE has grown considerably.

Adelaide real median household incomes have fallen by -13.1%, real threshold income for the lowest two income quintiles has fallen by 15.6% whilst real AWE just fell by -2.1%. For Melbourne the figures are -11.2% -11.7% and +0.6% respectively, whilst for Sydney they are, -4.1%, -5% and +2.5% respectively.

This suggests that whilst households in all capital cities seem to be losing purchasing power, those in the smaller centres appear to be losing it the fastest.

1.3 Unemployment and Employment Conditions

Graph 5 sets out the full-time unemployment rates for South Australia, Victoria and New South Wales (NSW), for the period 1986-2000.
Unemployment rates in both South Australia (8.4%), and Victoria, (6.2%), are at their lowest levels for a decade, whilst those in NSW have fallen to the lowest level of the last 14 years, (5.2%). However whilst full-time employment is relatively high and AWE is rising faster than the CPI household incomes are not keeping pace. Campbell\(^2\) and other researchers have identified the shift from low paid permanent employment to full-time casual employment, and the notion of rapid ‘job rotation’ amongst unskilled persons. There is therefore increasing evidence of the development of a group of households, who whilst in full-time employment, would not meet the credit criteria of major lending institutions and are now effectively precluded from home ownership (even though the incomes might suggest a capacity to pay the requisite mortgage requirements).

1.4 Dwelling Prices and Residential Rents

Table 2 sets out median dwelling prices and rents for selected statistical sub-divisions in Adelaide, Melbourne and Sydney for the period June 1986 to June 2000.

---

### Table 2: Median Dwelling Prices and Weekly Rents For Three Bedroom Houses And One Bedroom Units In Adelaide, Melbourne And Sydney: June 1986 – June 2000

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>House</td>
<td>Units</td>
<td>House</td>
<td>Units</td>
</tr>
<tr>
<td>S. Adelaide</td>
<td>-</td>
<td>-</td>
<td>105.5</td>
<td>94.1</td>
</tr>
<tr>
<td>N. Adelaide</td>
<td>65.0</td>
<td>60.4</td>
<td>85.7</td>
<td>67.9</td>
</tr>
<tr>
<td>W. Adelaide</td>
<td>-</td>
<td>-</td>
<td>107.3</td>
<td>92.8</td>
</tr>
<tr>
<td>E. Adelaide</td>
<td>98.9</td>
<td>80.2</td>
<td>157.6</td>
<td>119.7</td>
</tr>
<tr>
<td>N. W. Melbourne</td>
<td>-</td>
<td>0.0</td>
<td>112.5</td>
<td>90.9</td>
</tr>
<tr>
<td>Inner Melbourne</td>
<td>104.7</td>
<td>68.7</td>
<td>182.5</td>
<td>117.8</td>
</tr>
<tr>
<td>Inn. E. Melbourne</td>
<td>-</td>
<td>-</td>
<td>170.8</td>
<td>130.1</td>
</tr>
<tr>
<td>S. E. Melbourne</td>
<td>73.5</td>
<td>62.2</td>
<td>104.1</td>
<td>87.0</td>
</tr>
<tr>
<td>Sydney City</td>
<td>-</td>
<td>-</td>
<td>345.0</td>
<td>245.0</td>
</tr>
<tr>
<td>Inner City</td>
<td>89.5</td>
<td>84.0</td>
<td>160.5</td>
<td>130.0</td>
</tr>
<tr>
<td>Eastern Suburbs</td>
<td>160.0</td>
<td>84.0</td>
<td>279.0</td>
<td>162.0</td>
</tr>
<tr>
<td>Outer South West</td>
<td>66.0</td>
<td>65.0</td>
<td>128.0</td>
<td>110.0</td>
</tr>
<tr>
<td>Outer West. Syd.</td>
<td>61.8</td>
<td>51.9</td>
<td>93.5</td>
<td>72.5</td>
</tr>
<tr>
<td>Horn./Ku-ring-gai</td>
<td>160.5</td>
<td>69.0</td>
<td>270.0</td>
<td>185.0</td>
</tr>
</tbody>
</table>

### Median Weekly Rents

<table>
<thead>
<tr>
<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>House</td>
<td>Units</td>
<td>House</td>
<td>Units</td>
</tr>
<tr>
<td>N. Adelaide</td>
<td>100</td>
<td>50</td>
<td>135</td>
<td>80</td>
</tr>
<tr>
<td>E. Adelaide</td>
<td>110</td>
<td>60</td>
<td>160</td>
<td>85</td>
</tr>
<tr>
<td>Inner Melbourne</td>
<td>-</td>
<td>-</td>
<td>246</td>
<td>105</td>
</tr>
<tr>
<td>S. E. Melbourne</td>
<td>-</td>
<td>-</td>
<td>150</td>
<td>90</td>
</tr>
<tr>
<td>Inner City</td>
<td>120.2</td>
<td>112.8</td>
<td>215.5</td>
<td>135.0</td>
</tr>
<tr>
<td>Eastern Suburbs</td>
<td>140.8</td>
<td>112.8</td>
<td>245.5</td>
<td>112.0</td>
</tr>
<tr>
<td>Outer West. Syd.</td>
<td>70.6</td>
<td>59.3</td>
<td>95.0</td>
<td>63.0</td>
</tr>
</tbody>
</table>

Source: Valuer Generals Department South Australia and Victoria; Residex P/L City Return Reports
RP Data Special Data Run; Tenancies Branch, Department of Human Services, South Australia; Victorian Office Of Housing, Rental Reports; NSW Department of Urban Affairs And Planning Rent Reports

The above data indicate that for most inner locations and for single dwelling houses both prices and rents have grown significantly. However both prices and rents of one bedroom units on the fringe of metropolitan areas (eg in Northern and Western Adelaide) have tended to become somewhat more affordable in real terms.

### Real House Price Growth

**Inner Metropolitan Houses and Units**

Graphs 6, 7 and 8 set out real house and unit price growth for houses in inner metropolitan areas of Adelaide, Melbourne and Sydney.
GRAPH 6


Source: Valuer Generals Department South Australia
It is very clear from this analysis that real prices of both large and small dwellings in all inner metropolitan locations are increasing very significantly and much faster than real household incomes. Only unit prices in Eastern Adelaide are increasing at a pace closer to CPI increases.

**Outer Metropolitan Houses and Units**

There is however a somewhat different picture developing for real dwelling price growth in lower priced fringe areas of our capital cities. Graphs 9, 10 and 11 set out the results.
GRAPH 9


Source: Valuer Generals Department: South Australia
Of all the locations and types of dwellings examined only one bedroom unit prices in North Adelaide and South East Melbourne are growing at real rates at or below the rate of growth of household incomes. The question then becomes to what extent has the fall in both nominal and real interest rates offset the loss of affordability occasioned by real dwelling price rises. This is reviewed in the Housing Affordability section of the Report.
Real Residential Rent Growth:

*Inner Metropolitan Houses and Units*

Graphs 12, 13 and 14 set out the same analysis for rents in inner metropolitan areas.

Only for three bedroom houses in Inner Melbourne are rents increasing at rates at or below median household income growth. Whilst the rate of growth of rents for one bedroom units is slightly less severe than that for houses it is still considerably in excess of real median household income increases.

**GRAPH 12**

ADELAIDE: CPI, HOUSEHOLD INCOMES, AVERAGE WEEKLY EARNINGS AND EAST ADELAIDE RENTS. 1986 - 2000

Source: Tenancies Branch, Department of Human Services, South Australia
GRAPH 13
MELBOURNE: CPI, HOUSEHOLD INCOMES, AVERAGE WEEKLY EARNINGS AND INNER MELBOURNE RENTS: 1986 - 2000

Source: Victorian Office Of Housing, Rental Reports

GRAPH 14
SYDNEY: CPI, HOUSEHOLD INCOMES, AVERAGE WEEKLY EARNINGS AND INNER CITY SYDNEY RENTS: 1986 - 2000

Residex P/L City Return Report; NSW Department of Urban Affairs And Planning Rent Reports

Outer Metropolitan Residential Rents

Graphs 15, 16 and 17 set the same analysis for rents for lower priced outer metropolitan areas.
GRAPH 15


Source: Tenancies Branch, Department of Human Services, South Australia

GRAPH 16


Source: Victorian Office Of Housing, Rental Reports
These graphs demonstrate that rent prices are growing much faster than household incomes in Outer Western Sydney, slightly faster for houses in North Adelaide, slightly slower for units in North Adelaide and much slower for both houses and units in South East Melbourne. Hence it can be suggested that only in South Eastern Melbourne has the affordability of renting significantly improved.

**Real Percentage Growth of Dwelling and Rent Prices**

Graphs 18 and 19 set out the real percentage change in house and unit prices for the seven metropolitan locations examined.
South Eastern Melbourne and both Adelaide locations experienced real house price falls in the period 1991-96 with the falls exceeding -10% in South East Melbourne. However in the most recent period, (1996-2000) all locations have experienced very significant real price growth, varying from a high of 53.2% for median prices of houses in Inner City Sydney to a low of 12.9% in North Adelaide. In all locations other than the aforementioned, real median houses prices have increased by more than 20%, and in five of the seven by more than one third.

Graph 19 sets out the same analysis for median one-bedroom unit prices.
Unit prices in Northern Adelaide have had an extended period of falling real prices, and have fallen by nearly -9% in the last four years. Similarly during the period 1991-1996 real unit prices fell sharply in South Eastern Melbourne (-17%), and slightly in Eastern Adelaide, (-3.3%). In the last four years however, real unit prices have increased by more than one third in all Melbourne and Sydney inner locations and by more than 11% in Eastern Adelaide. Even on the low cost locations on the fringe of Sydney and Melbourne one-bedroom unit prices have increased by approximately 10% or more, (although in South Eastern Melbourne this has not compensated for the 17% fall over 1991-1996).

Graph 20 sets out the same analysis for real house rents.

During the period 1991-1996 real median three bedroom house rents fell slightly in North Adelaide, (-4.7%) and moderately in South East Melbourne, (-8.1%). Over the period 1996-2000 there were further slight negative real rent changes in Inner Melbourne, (-3.7%). In other locations the period 1991-1996 was characterised by very rapid real rent rises, ranging from a high of 67% in Outer Western Sydney, to a low of 0.5% in Eastern Adelaide, with all Melbourne and Sydney inner metropolitan locations experiencing increases in excess of 20% and all Sydney locations (outer and inner) increases in excess of 40%. Since 1996 the rate of real house rent increases has moderated with Inner Sydney and Eastern Adelaide experiencing the largest increases, (15% and more), Outer Western Sydney more than 10% and fringe Adelaide and Melbourne locations less than 7%.
ADELAIDE, MELBOURNE AND SYDNEY: PERCENTAGE CHANGE IN REAL MEDIAN HOUSE RENTS: 1986-2000

Source: Tenancies Branch, Department of Human Services, South Australia; Victorian Office Of Housing, Rental Reports; Residex P/L City Return Reports; NSW Department of Urban Affairs And Planning Rent Reports

Graph 21 sets out the same analysis for one-bedroom units.

ADELAIDE, MELBOURNE AND SYDNEY: PERCENTAGE CHANGE IN REAL MEDIAN UNIT RENTS: 1986-2000

Source: Tenancies Branch, Department of Human Services, South Australia; Victorian Office Of Housing, Rental Reports; Residex P/L City Return Reports; NSW Department of Urban Affairs And Planning Rent Reports

During the period 1986-1991 real median unit rents fell significantly in Sydney, (between -10% and -26%), and rose by 20% in North Adelaide. (note no data was available for Melbourne). This trend was traumatically reversed in the period 1991-1996 where real median unit rents increased by in excess of 50% in parts of Sydney, but fell by more than one third in South East Melbourne and by -20% in Northern Adelaide. Since 1996 the previous rapid fall in South Eastern Melbourne has been compensated by a nearly 50% increase with approximately a 30%
increase in inner metropolitan locations of Sydney, and approximately 17% in Adelaide. In this period overall real rents increased slowest in Outer Western Sydney, (6.6%).

1.5 Median Mortgage and Rent Payments

Table 3 sets out the median mortgage and rent actually paid by households in Adelaide, Melbourne and Sydney over the period 1986-1996.


<table>
<thead>
<tr>
<th>Year</th>
<th>Adelaide</th>
<th>Melbourne</th>
<th>Sydney</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Median Monthly Mortgage Payments (Actual Paid)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1986</td>
<td>288.23</td>
<td>340.34</td>
<td>394.58</td>
</tr>
<tr>
<td>1991</td>
<td>489.34</td>
<td>603.71</td>
<td>686.39</td>
</tr>
<tr>
<td>1996</td>
<td>763.64</td>
<td>805.77</td>
<td>1016.55</td>
</tr>
<tr>
<td></td>
<td>Median Weekly Rent Payments (Actual Paid)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1986</td>
<td>82.15</td>
<td>90.11</td>
<td>99.41</td>
</tr>
<tr>
<td>1991</td>
<td>115.23</td>
<td>133.20</td>
<td>165.45</td>
</tr>
<tr>
<td>1996</td>
<td>129.92</td>
<td>142.86</td>
<td>188.50</td>
</tr>
</tbody>
</table>

Excludes Not Applicable and Not Stated

As is to be expected, Adelaide has the lowest median mortgage and rent payments followed by Melbourne and then Sydney. In the period 1986-1991 median rent payments increased substantially in Sydney, whilst median mortgage payments grew by around 30% in real terms for all capital cities examined. Between 1991 and 1996 rent repayment increases were modest, but mortgage repayments grew very fast in both Adelaide and Sydney.

Graph 22 sets out the real percentage change for these payments between 1986 and 1991 and for the period 1991 to 1996.

Between 1986 and 1991 real median mortgage payments increased by nearly one third in Melbourne, and by nearly 30% in Sydney and 26% in Adelaide. With the exception of Sydney, (24%), real median rent growth was more modest, not exceeding 10%.
Between 1991 and 1996 real growth in median mortgage payments accelerated even further, increasing fastest in Adelaide, (43.4%), followed by Sydney (36%), and Melbourne, (22.6%). Real median rent payment growth was however very modest, increasing by less than 5% in Adelaide and Sydney and being negative in Melbourne.

It is obvious that a substantial component of the increases in real median mortgage growth is being fuelled by dwelling price increases, but is also likely that as the nature of home loan financing has changed many households may have taken advantage of the efficiencies offered by home loan rates by consolidating their other debt commitments into the household mortgage. Of more interest however is the fall in the rate of growth of median rent payments, which may have responded to the increasing supply of rental accommodation generated by urban consolidation policies. It does appear that the trend has been reversed in the last four years.

### 1.6 Tenure Change

Graph 23 sets out for Adelaide, Melbourne and Sydney the percentage change in the proportion of total households privately renting over the periods 1986-1991 and 1991-1996.
One of the consequences of declining purchase affordability should be a shift in the proportions of households owning/purchasing and renting.

In a perfectly rational market, (which housing is not), there should be an almost direct correlation between the rate of increase in dwelling prices and the shift to proportions of households privately renting. The graph above indicates that the proportion of households privately renting is increasing fastest where there have been the most severe dwelling price increases. For example over the latter five year period, the proportion of Melbourne households privately renting increased by not quite 11% whereas that for Sydney grew by nearly 20%.

1.7 Residential Mobility or the Frequency of Residential Relocation

The frequency with which owner/purchasers move their home location impacts on the demand for housing and hence long term price growth. The more frequently home owners move the greater the activity in the market and greater the aggregate demand for home ownership. There is now statistical evidence, that the rate at which owner/purchasers are moving is in fact slowing and between 1986-1991 and the 1991-96, the average length of stay increased from seven to nine years. Over the very long term this may dampen price growth.
2  Housing Affordability And Housing Stress

2.1  Housing Affordability

The National Housing Strategy (NHS) defined affordable housing as a situation that:

....conveys the notion of reasonable housing costs in relation to income: that is, housing costs that leave households with sufficient income to meet other basic needs such as food, clothing, transport, medical care and education

The NHS distinguishes between ‘accessibility’, viz

‘....i.e. the cost of becoming a home purchaser or entering a rental arrangement’

and affordability

‘....i.e. the ongoing cost of housing in relation to gross income’.3

The NHS suggests the most commonly used affordability measure in housing research is the ratio of housing costs to income. Leaving aside the costs of access, housing costs vary according to the type of tenure considered; in the case of home ownership the main costs will be the cost of mortgage payments, plus the cost of maintenance and rates, whereas in public rental tenure the costs are normally limited to the payment of the rent.

The National Housing Strategy was particularly concerned to point out that those income units in the lowest 40 per cent of gross income distribution could not be expected to pay more than 25 per cent of their income in rent if they were to be left with sufficient funds to meet their other needs adequately.4 The Strategy also indicated that, if required, a more conservative (but less ‘adequate’) benchmark would be 30% of income in housing payments (rent or mortgage) for income units in the lowest 40% of gross income distributions. This also coincides with the maximum acceptable mortgage repayment limits set by institutional mortgage providers.

The Senate Committee Report on Housing Assistance said:

The NHS approach has been criticised in some quarters as being too rigid and unrelated to what different households, especially those in crisis, need to spend on essential non-housing costs.

In its more recent work in the area of housing affordability, the Australian Institute of Health and Welfare (AIHW) has developed a more sophisticated model taking into account differences in the size of the household, its composition and location in determining the proportion of income that household can afford to spend on housing.

While the AIHW model has much to recommend it because of its sensitivity to differences in the financial situations of low income households, the Committee recognises that the adoption of such a model would pose major problems of administration for a government department.5

In its research on households experiencing affordability problems the NHS found that only 5.7% of full home owners and 4.8% of government renters were in housing ‘stress’ (paying more than

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5 REPORT OF THE PARLIAMENTARY SENATE COMMUNITY AFFAIRS REFERENCE COMMITTEE, December 1997, Housing Assistance In Australia (pp 1 -2)
30% of household income for housing costs). The most recent housing survey carried out by the Australian Bureau of Statistics (1999) found that the proportion of outright home owners paying more than 30 per cent in housing costs was 4.9 per cent. The figures for purchasing owners, public tenants and private tenants were 27.9 per cent, 9.9 per cent and 54.7 per cent, respectively. Changes in Australia’s financial sector during the last 15 years have resulted in large and increasing flows of savings into financing home ownership. The rapid recent growth in the secondary market for residential mortgages underscores the relative neglect of the private rental sector, especially by large corporate investors. Capital constraints on both public borrowing for public housing and investment in private rental housing is contributing to the worsening affordability problems being experienced in the private rental sector. Consequently, the need for innovative policy interventions is likely to be most needed in this sector and this forms the focus for this report.

Consequently this analysis is confined to private renter households and, in the absence of other fully accepted models, uses 30% of gross household income as the affordability benchmark.

This chapter examines a number of major questions: These are:

- over the period 1986-2000 how has affordability changed for all private renters?
- what can lower income (i.e. lower two income quintiles) private renter households currently afford?
- to what extent is there any affordable and appropriate housing choice for lower income renters? and
- what can’t lower income private renter households afford.

**Affordability Trends**

Given the data available we have analysed the minimum household incomes required to buy or rent three bedroom houses and one bedroom units in the locations specified earlier.

The assumptions are for:

- home purchase; a deposit accounting for 5% of purchase price and ancillary transaction costs, a twenty five year credit foncier standard bank loan (based upon the prevailing bank interest rate at the time, i.e. June 1986, 1991, 1996 and 2000), and 30% of gross income in repayments; and

- private rental; a maximum of 30% gross income in rent payments.

We have then analysed the proportion of private renters in each of the capital cities who had the minimum incomes required to rent or buy affordable housing at June 1986, and compared this with the proportions able to do so in 1991, 1996 and 2000.

Graph 24 sets out the results.
Between June 1986 and June 2000 the proportion of all private renter households in each capital city who could afford to:

- rent one bedroom units;
  - has declined slightly in East Adelaide (-5.4% fewer renter households), Inner City Sydney (-4.4%) and Outer Western Sydney (-1.4%), and substantially in Inner Melbourne (-11.2%);
  - increased slightly in North Adelaide (+2.06%), and substantially in South Eastern Melbourne (+12%);

- rent three bedroom houses;
  - declined slightly in Eastern Adelaide (-8.6%), and Inner Melbourne (-1.6%), and very substantially in Inner City Sydney (-27.5%) and Outer Western Sydney (-18.6%);
  - increased moderately in North Adelaide (6.4%), and South Eastern Melbourne (8.7%);

- buy one bedroom units:
  - declined very marginally in Inner Melbourne (-2.3%), and Inner City Sydney (-0.94%); and
  - increased substantially in Eastern Adelaide (20.7%), North Adelaide (50.7%), South Eastern Melbourne (35%), and Outer Western Sydney (25%);

- buy three bedroom houses:
  - declined moderately in Inner City Sydney (-4.8%), and Outer Western Sydney (-7.1%);
  - increased slightly in Eastern Adelaide (7%), and Inner Melbourne (1.9%), and increased substantially in North Adelaide (21.8%), and South Eastern Melbourne (23.8%).

Overall for Adelaide:
• affordability has improved for all types of dwellings and tenures in North Adelaide, and purchasing dwellings in East Adelaide.

Overall for Melbourne:

• affordability has only improved for buying houses in Inner Melbourne, but for all dwellings and tenures in South Eastern Melbourne.

Overall for Sydney:

• affordability has declined for all types of dwellings and for both renting and buying with the exception of buying one-bedroom units in Outer Western Sydney.

2.2 Affordability for Low Income Private Renters

The above findings are of course based on all private renters. The major issue is what can those on incomes just below median household incomes (i.e. the lowest 40%) afford?

By adjusting the 1996 Census lowest 40% household incomes by AWE, the above exercise was applied to June 2000 house prices and rents. Graph 25 sets out the results.

The analysis demonstrates that for private renters in the bottom two income quintiles:

• no households can affordably buy an average (median) priced three bedroom house in any metropolitan location;
• 39% of Adelaide’s and 15% of Melbourne’s salient households can afford to buy an average one bedroom unit in North Adelaide or South East Melbourne, with no households in Sydney being able to purchase average one bedroom unit anywhere in the metropolitan area;
• 9% of Adelaide’s, and 3% of Sydney’s salient households can afford to rent an average three bedroom house in either South East Melbourne or Outer Western Sydney only, with no households being able to rent an average three bedroom house in any Melbourne location;
• over 50% of salient households from each capital city can afford to rent an average one bedroom unit in the outer locations, (North Adelaide, South Eastern Melbourne and Outer Western Sydney);
• a very small proportion of households are able to afford to rent an average one bedroom unit in inner Melbourne or Sydney locations (5%, Inner Melbourne only); and 38% of households can afford the rent of the average one bedroom unit in East Adelaide.
To sum up, low income private renter households have very, very limited affordable housing choices; both by location and dwelling type. Moreover, where a small degree of choice appears to exist – viz. renting a one bedroom unit on the fringe – this ignores the question of appropriateness. Clearly this only represents a choice for small households.

2.3 Housing Stress

Housing ‘stress’ is defined by the National Housing Strategy as:

‘Income units are said to be in financial housing stress if they pay more than 30% of income on housing and are in the lowest (40%) of the income distribution range.’

There has been considerable discussion about the need to take account of after-tax disposable income rather than before tax or gross income.

Other arguments have related to the concept of housing related poverty and the development of a methodology which is pertaining to whether or not an income unit can be said to be experiencing poverty ‘before’ and ‘after’ housing costs. In the context of this analysis we have used the gross income measure.

For this analysis we have examined those in the lowest two household income quintiles, and also the total private renter households experiencing housing related stress according to the definition outlined above. We have analysed the outcomes longitudinally over the Censi 1986 to 1996.


Lowest 40% Of Household Incomes

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Graph 26 sets out for 1986 and 1996 the proportion of private rent paying households (household incomes in the lowest 40% of all household incomes) experiencing housing stress.

Between 1986 and 1996 private rent paying households in housing related 'stress' (household incomes in the lowest 40% of household incomes), as a proportion of total private renter households with the same income distributions grew/fell for:

- Adelaide from 63.4% to 76.1;
- Melbourne from 60.5% to 74%;
- Sydney from 67.3% to 80.7%;
- Brisbane from 63.7% to 64.3%;
- Perth from 59.9% to 56.1%;
- Hobart from 57.7% to 62.4%;
- Darwin from 70.7% to 63.7%; and
- the average for all capital cities from 64.1% to 72.7%

In the state capital cities of Australia nearly 3 out of every 4 private renter households (with incomes in the lowest two income deciles) are now experiencing housing stress.

This represented 227,480 households. If the provision of new physical dwellings is applied to secure the necessary affordable housing for this large sub-group, the total cost would be $27.24 billion. (The capital requirement has been calculated according to the assumptions set out in Attachment 1.) This is a conservative estimate because the estimated costs are the latest available 1998/99 figures, whilst the total shortfall does not of course include stressed households in regional Australia.

Other solutions such as providing additional Rent Assistance or subsidising home loan interest rates would of course cost much less in the short run (and possibly somewhat less in the longer term) but would require further analysis to clarify exact costs. However, some general pointers can be outlined. In many circumstances rent assistance might not be the best way to achieve the provision of affordable housing. For example, if rent yields are high and loan interest rates are lower it might be more cost effective to subsidise home purchase. Alternatively, if rent yields are very high and housing prices have fallen substantially the provision of new public rental housing might be most suitable. In cases where prices remain buoyant, rent yields are low and housing interest rates are moderate, shared equity may have the best cost/risk profile.
The increase in the number of private renter households in the capital cities with household incomes in the lowest 40% of all household incomes and experiencing housing stress was:

- 7,400 in Adelaide;
- 22,600 in Melbourne;
- 28,600 in Sydney;
- 17,600 in Brisbane;
- 9,900 in Perth;
- 1,800 in Hobart;
- 1,000 in Darwin, and
- 90,000 across all capital cities.

Graph 27 sets a comparison of the growth in total households in this category with households in stress.
GRAPH 27

Source: ABS: Census of Population and Housing: Special Cross Tabulation of Table B57. Excludes Partial Incomes and No Incomes Stated.

In five out of the seven capital cities, stressed households are growing more rapidly than total renter households in the same income categories, having increased by:

- 69% in Adelaide, compared to 26% for all renter households in the category;
- 62% in Melbourne, compared to 32.7;
- 49% in Sydney compared to 24.4%;
- 99.3% in Hobart compared to 84%; and
- 103% in Brisbane compared to 101.6%.

In Darwin and Perth the rate of growth of stressed households was slightly less than the overall rate of growth for households in the same income categories.

Total Private Rent Payers

Graphs 28 sets out total private renters paying more than 30% of income in rent as a proportion of all private rent paying households.

GRAPH 28

GROWTH IN PRIVATE RENT PAYING HOUSEHOLDS (incomes within lowest two household income deciles) PAYING MORE THAN 30 % OF INCOME IN RENT COMPARED TO GROWTH IN TOTAL RENTER HOUSEHOLDS IN SAME INCOME CATEGORIES: 1986 - 1996
In the seven capital cities total private rent payers experiencing stress grew by:

- 7,300 households in Adelaide;
- 27,600 households in Melbourne;
- 47,350 households in Sydney;
- 20,580 households in Brisbane;
- 11,200 households in Perth;
- 1,700 households in Hobart; and
- 860 households in Darwin.

The total increase in stressed renter households for all capital cities and Darwin was 116,750.

These increases represented a:

- 55% increase in Adelaide;
- 71% increase in Melbourne;
- 74% increase in Sydney;
- 100% increase in Brisbane;
- 70% increase in Perth;
- 76% increase in Hobart;
- 82% increase in Darwin, and
- a 74% increase across all capital cities.

The increase in housing stress has occurred during a period of generally high economic growth. Graph 29 compares GDP growth over the 1986-1996 period with the growth in numbers experiencing housing stress for all capital cities. It is clear from this graph that the growth in numbers in housing stress is not inversely correlated with GDP.
In Australian capital cities (if the rate of growth of stressed households experienced in the last 10 years continues) then the number of households experiencing stress will double in fifteen years and reach nearly one million within 20 years. Furthermore, this analysis probably understates the problem because it ignores the growth in stressed households in regional Australia. Recent research carried out by Yates and Wulff (disaggregating their national-level analysis noted in the Introduction) suggests that effective shortages of low cost rental dwellings are even more intense in regional Australia, where incomes at the bottom end have fallen significantly.

Of major concern is the very rapid rate at which housing stress appears to be reaching well into middle income renter households, and this is the most rapidly growing aspect of housing stress. Some higher income households will choose to commit a higher proportion of their incomes to housing and be able to afford it. However, other tenants may be struggling and reasonably said to be suffering housing stress. This suggests that housing affordability problems may be climbing the income ladder, affecting not only unemployed and under-employed people but those who have been described as the ‘working poor’ and even middle income households.

This broader view of the impact of intensifying housing stress raises the prospect of ‘social exclusion,’ which refers to the concentration of households with multiple disadvantages, including inadequate housing, in particular areas. The hallmark of excluded communities is disconnection from the mainstream institutions and opportunities in society, including access to

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8 A recent study points to the scale of the problem in the U.S. Stegman et al. (2000) found that of the 13.7 million households who were paying more than 50 per cent of their incomes in housing costs, or otherwise living in sub-standard housing, 3 million or more than 20 per cent were working families. Particularly vulnerable were occupations like teachers and police officers. Some regions had more than twice the national average of households in this dire situation, creating major problems for those regional economies in attracting low paid workers. These numbers would, of course, increase substantially if the NHS benchmark of 30 per cent was used.
jobs, services and decent housing. Housing situation acts as one important factor in perpetuating this state of affairs.  

2.4 Why Rent Assistance (by Itself) is Not Enough

It may be acknowledged by Government and others that housing affordability is declining rapidly at least in the majority of the major metropolitan locations around Australia. However, some proponents of demand side responses might suggest that all the Commonwealth Government needs to do in response is to broaden the rent and eligibility criteria available under the current Rent Assistance (RA) program. That is, it might be argued that housing affordability problems can be adequately managed by sufficiently expanding the rent assistance program.

This section:
- briefly outlines the characteristics of the Commonwealth Government’s current Rent Assistance Program, and;
- comments upon the:
  ⇒ efficiency;
  ⇒ effectiveness;
  ⇒ equity; and
  ⇒ cost and risk implications associated with such a policy response.

The broad conclusion reached is that, by itself, RA is not adequately meeting the challenge, nor is it likely to in the future, given the current constraints on government expenditure.

**Characteristics of the Rent Assistance Program.**

The Commonwealth Government outlays approximately $1.6 billion per annum for the provision of Rent Assistance throughout Australia.

In a report examining measurement and data issues attaching to the Rent Assistance program the Australian Institute of Health and Welfare attempted to define what Rent Assistance is

Rent Assistance is a non-taxable cash payment to Commonwealth clients who rent accommodation in the private rental market. The payment is available to all pensioners, allowees, beneficiaries and family payment recipients who pay rent above minimum threshold levels and is provided at the rate of 75 cents per dollar of rent paid above these thresholds up to specific maximum rates of assistance. Both the rent thresholds and the maximum rates of assistance are indexed twice yearly and vary with both family type and the presence and number of children) (Karmel, 1988, p. 160).

Rent Assistance is available to individuals who:

- receive a pension;
- receive more than the base rate of Family Tax Benefit with dependent children;
- don't have dependent children and receive an allowance or benefit; and
  ⇒ are over 25, or
  ⇒ are partnered, or
  ⇒ are under 25 (under 21 if receiving Disability Support Pension) and living permanently, or indefinitely apart from parents or guardians.

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9 For a fuller discussion of this issue see Berry (2000a).
Individuals or households must also be paying more than a certain amount for:

- rent (other than for public housing); or
- service and maintenance fees in a retirement village; or
- lodging; or
- fees paid to use a site for a caravan or other accommodation which are occupied as the principal home; or
- fees paid to moor a vessel occupied as the principal home.

Eligibility for Rent Assistance is assessed when claiming a pension, allowance or benefit.

Payment rates effective from 20 March 2001 are listed in Table 4.

### Table 4
Rent Assistance Rates with No Dependent Children

<table>
<thead>
<tr>
<th>Situation</th>
<th>Maximum payment per fortnight</th>
<th>No payment if your fortnightly rent is less than</th>
<th>Maximum payment if your fortnightly rent is more than</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single, no dependent children</td>
<td>$88.00</td>
<td>$78.00</td>
<td>$195.33</td>
</tr>
<tr>
<td>Single, sharer, no dependent children</td>
<td>$58.70</td>
<td>$78.00</td>
<td>$156.27</td>
</tr>
<tr>
<td>Couple, no dependent children</td>
<td>$82.80</td>
<td>$127.00</td>
<td>$237.40</td>
</tr>
<tr>
<td>One of a couple who are separated due to illness, no dependent children</td>
<td>$88.00</td>
<td>$78.00</td>
<td>$195.33</td>
</tr>
<tr>
<td>One of a couple who are temporarily separated, no dependent children</td>
<td>$82.80</td>
<td>$78.00</td>
<td>$188.40</td>
</tr>
</tbody>
</table>

Source: Centrelink, 2001

### Table 5:
Rent Assistance Rates with Dependent Children

<table>
<thead>
<tr>
<th>Family Situation</th>
<th>Maximum payment per fortnight</th>
<th>No payment if your fortnightly rent is less than</th>
<th>Maximum payment if your fortnightly rent is more than</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single, 1 or 2 children</td>
<td>$103.04</td>
<td>$102.62</td>
<td>$240.01</td>
</tr>
<tr>
<td>Single, 3 or more children</td>
<td>$116.48</td>
<td>$102.62</td>
<td>$257.93</td>
</tr>
<tr>
<td>Couple, 1 or 2 children</td>
<td>$103.04</td>
<td>$151.90</td>
<td>$289.29</td>
</tr>
<tr>
<td>Couple, 3 or more children</td>
<td>$116.48</td>
<td>$151.90</td>
<td>$307.21</td>
</tr>
</tbody>
</table>
Rent Assistance is *not* paid:

- to people paying rent to a government housing authority, although in some situations sub-
tenants may qualify for Rent Assistance;
- for residents of Commonwealth funded nursing homes and hostels;
- to single disability support pensioners under 21, without dependants, living with parents;
- to other single people under 25, living with parents; and
- to students without dependants, who receive Austudy Payment.

Special rules apply to single sharers, people who pay board and lodging or live in a retirement village.

Where both members of a couple without children are receiving an allowance or benefit, Rent Assistance is shared.

**The Efficiency of Rent Assistance**

Economic efficiency can be divided into three component parts:

- *technical or productive efficiency* is achieved when goods and services are produced and supplied to consumers at least cost. In the case of housing, this refers to the ability of builders and housing developers to build and supply houses at an efficient cost;

- *allocative efficiency* is achieved where resources used to produce a set of goods or services are allocated to their highest valued uses, that is, uses that provide the greatest benefit relative to costs; put another way, allocative efficiency is achieved where it is not possible to make some people better off without making others worse off; and

- *dynamic efficiency*, which reflects the need for firms to make timely changes to their products in response to changes in technology and consumer tastes.

There is evidence that the existing housing market may be deficient in respect of dynamic and allocative efficiency. In most cases, competitive markets are able to generate efficient outcomes in the supply of goods and services. An exception to this is when there is the existence of “market failure”. Market failure occurs when a market has particular features or characteristics that prevent or restrict its efficient operation by distorting the price signals sent to producers and consumers. There are a number of causes of market failure such as the existence of externalities, monopolies, imperfect information or public goods. Few, if any, markets are perfectly efficient and the residential rental property market has more imperfections than most.

Under the conventionally accepted assumptions of economic theory the price of a commodity is a function of the demand and supply relationship. When a good is in short supply relative to its demand, its price will rise. This, in turn, will create unusually high profits, encouraging additional production of the scarce commodity. Supply then increases, and prices are once again bid down to a new equilibrium level.

Thus, the economically conventional proponents argue, increasing the demand for rental housing via Rent Assistance will not result in bidding up rent prices and windfall gains for landlords. They argue that market processes ensure:

1. that Rent Assistance is an efficient means of delivering housing assistance because the rental housing market is an efficient market; and therefore,

2. as demand for rental housing is stimulated through the provision of Rent Assistance, the supply of low cost rental accommodation will increase and rent prices will fall back to levels appropriate to an equilibrium position of supply and demand.
Gilderbloom and Applebaum (1987, p. 262), in an American study on the economics of private rental markets, argue:

Conventional economic models of housing markets and Rent Assistance Programs assume that urban housing rental markets are competitive and that rent levels are determined solely by the supply and demand for housing.

For example, Mills (1972:164) argues that the "supply of both new and used housing is competitive". Ingram et al. (1976:11) similarly maintain that the "housing market has much in common with the idealized competitive market portrayed in microeconomic theory. For example, the market is not concentrated and a large number of buyers and sellers participate in any metropolitan market".

Logically, therefore, if rental housing markets are not substantially efficient, increases in demand will not necessarily be matched by increases in supply, with 'super'-rents and some part of the Rent Assistance being captured as windfall gains by landlords.

**The Characteristics of an Efficient Housing Market**

Gilderbloom, J.I. & Applebaum (p. 262) discuss the characteristics of an efficient market and focus on seven points that Olsen (1973, pp. 228-29) enumerates as requisite conditions for supply to respond freely to changes in demand:

1. both buyers and sellers of housing services are numerous;
2. the sales or purchases of individual units are small in relation to the aggregate volume of transactions, and so do not by themselves significantly affect total supply;
3. neither buyers nor sellers collude;
4. both producers and consumers possess perfect knowledge about the prevailing price and current bids, and take advantage of every opportunity to increase profits; i.e. comprehensive information on asset performance is universally available and this information is available in "real time" i.e. as new information becomes available there is no significant delay in dissemination to the market.
5. housing services are an homogeneous commodity.
6. entry into and exit from the market is free for both producers and consumers;
7. no artificial restrictions are placed on demand for, supplies of, and prices of the bundle of housing services, or the resources used to provide such services; i.e. the commodity is both portable and liquid.

In relation to the real characteristics housing markets, we can make the following comments:

**Buyers and Sellers**

Economists regard rental housing markets as extremely dispersed in terms of ownership and market control. It is clear that renters fulfill the competitive assumption, they are typically numerous, unknown to one another, and compete fully with one another for housing. A similar condition exists for rental landlords (see chapter 4.2 for details).

**Sales and Purchases**

As a rule housing units are rented individually and it is difficult to conceive of a situation in most metropolitan rental housing markets where action by one entity would substantially affect the supply of private rental housing.

**No Collusion**

There is no evidence of any significant collusion between renters and landlords.
**Comprehensive, Real Time Information.**

Tenants’ knowledge of prevailing rents is usually based on fragmentary information obtained from newspaper advertisements, personal networks and general folklore. Since tenants are seldom in a position to devote much time to systematic data gathering, they often “make do” with whatever is available to them, especially if available units are scarce.

In the residential markets the quality of the information on capital losses or gains, rental yields and rental vacancies, cost structures etc is very variable and incomplete.

Because of the nature of the private rental market there are always significant delays between actual market developments and the availability of appropriate information on these developments (such as vacancy rates, rent increases/falls, supply changes etc). In metropolitan residential rental housing markets relevant information is never available in real time (i.e. as it occurs in the market).

**Homogeneous Housing Services**

Investments such as bonds and stocks are relatively homogenous, i.e. one bond in a particular issue has exactly the same characteristics as any other. By contrast, residential investments are heterogeneous, every dwelling is unique.

Housing is not a homogeneous commodity, in which all units are equivalent substitutes. A house or apartment is unique because of its amenities, size, architecture, age, quality, and neighbourhood. It would be difficult to find an exactly equal substitute for any particular house. As Olsen (1973:229) suggests, “most scholars would probably find [homogeneity) to be the least plausible assumption.” (Gilderbloom and Applebaum, 1987, p. 266).

**Absence of Barriers To Entry And Exit**

As Gilderbloom and Applebaum (ibid., p. 264) note there are many barriers to entry and exit for private renters:

Consumers of rental housing face many barriers to mobility. Most obvious are discriminatory practices of various sorts, which close off large segments of the housing market to families with children, racial minorities and the poor. Cherry and Ford (1975) and Rich (1984:39) show how racial discrimination in housing limits mobility within housing markets and leads to segmented sub-markets (also see Rose-Ackerman, 1977). As a result, lower income tenants pay proportionally more for rental units regardless of the quality of those units

Under competitive positions when the price of a product goes up the consumer has the choice of either reducing consumption or switching to a substitute product. With a basic necessity such as housing, the former option implies a reduction in the living standard, including fewer amenities, reduced maintenance, or some combination of the three.

The latter option is seldom available: few tenants can afford to buy homes or condominiums. Even the option of moving is seldom viable: comparably priced units are likely to be scarce and, in addition to the economic costs, moving entails such non-economic costs as Consumers of rental housing face many barriers to mobility. Most obvious are discriminatory practices of various sorts, which close off large segments of the housing market to families with children, racial minorities and the poor. Cherry and Ford (1975) and Rich (1984:39) show how racial discrimination in housing limits mobility within housing markets and
leads to segmented sub-markets (also see Rose-broken social ties, lost neighbourhood attachments, and the uprooting of children to different schools.

Yates and Whitehead (1998, p. 417) in an examination of supply side subsidies identify factors that inhibit the entry and exit of producers, i.e. landlords, commented:

….there has been a considerable amount of work undertaken at an aggregate rather than a sub-market level which has cast considerable doubt on the efficiency of housing markets. Gatzlaff and Tirtiroglu (1995), provide a comprehensive overview of this US based literature concluding that “transactions costs typically prohibit investors from exploiting the predictable price movements in any of the market segments”….  

Within the context of the same US market to which Apgar’s analysis applied, Malpezzi and Green (1996) suggest there is evidence of imperfections at the bottom end of the market. They attribute this partly to building codes which truncate filtering and partly to land use regulations which cause the bottom end of the market to malfunction….  

Lastly, there is a high degree of inertia on the part of home purchasers and owners, because of the high entry and exit costs associated with a move.

**Supply, Liquidity and Portability**

There is a considerable lag between the decision to sell a dwelling and the actual completion of a sale. Conversely, there is also a lag between the decision of developers and builders to increase supply and the availability of the stock, usually about nine months. Local government planning regulations and conflicts over local amenity can delay new residential developments for even longer periods. In circumstances where there may be a perceived shortage of dwellings in a particular market, the supply and demand relationship may well have changed before the additional stock is provided.

Whereas bonds are portable, i.e. easily moved and stored, and highly liquid, that is they can be instantly sold, dwellings are fixed in space and dwellings are also non liquid. Consequently housing suffers from supply lags and illiquidity.

**Conclusions**

Efficient pricing of housing markets, and in particular rental housing markets, is therefore impeded by:

- imperfect information;
- information lags;
- product heterogeneity;
- consumer discrimination;
- inertia caused by entry/exit costs;
- supply lags and supply distortion due to regulation;
- spatial fixity, i.e. lack of portability; and
- illiquidity.

**Demand Incentives and Supply Responses**

If housing markets are efficient, in allocative terms, then there should be some evidence of supply responses to demand incentives such as Rent Assistance or Housing Allowance type programs.
Agar (1990, p.1) in his examination of the arguments applying to different housing assistance policies cautions:

Housing vouchers or similar demand subsidies may be appropriate in some contexts but economic theory and recent empirical analysis suggest that such subsidies are “not the best at all times and under all situations”. Rather the best policy depends on program targeting and the nature and extent of program induced price increases and externality effects.

Some early American experiences with Housing Allowances -- such as the Housing Allowance Demand Experiment (HADE) in Pittsburgh, Pennsylvania and Phoenix, Arizona -- might suggest that there is no evidence of price effects from the introduction of Rent Assistance or allowances.

Agar (ibid., p. 7, p. 11) suggests, however, that such conclusions cannot be drawn from the HADE results:

The experimental nature of the program may have led recipients to treat the allowance as a “windfall” rather than as a permanent addition to income. If recipients do not view the assistance as a more permanent addition to income the demand response i.e. increased housing consumption is likely to be very limited.

And

In metropolitan areas characterized by significant disinvestment in selected neighbourhoods, a housing allowance program could further destabilize the housing market by further inducing households to move out of areas with high vacancy rates and low-quality housing and move into areas with low vacancies and strong upward pressure on rents. In this context, a housing allowance arguably could both add to abandonment pressures in some neighbourhoods and stimulate excess demand pressures in other neighbourhoods and still not evoke, at least in the short run, a positive supply response that would limit price increases.

Yates and Whitehead (1998, p. 417) evoke similar conclusions:

Freeman’s (1997) work on cross-national comparison of tenure patterns, for example, suggests that the size of the private rental sector is influenced by whether demand or supply side subsidies are employed. There is no association between the presence of demand-side subsidies and a large private rental sector, but there is some association between supply-side subsidies and the existence of a large private rental sector. Whilst this is not conclusive, such an observation does reinforce a concern with the capacity of the private rental sector to respond to demand side subsidies.

Ermish (1984, pp. 78-79) in his work for the Joseph Rowntree Trust examined the way in which housing and tax policies influence the cost of housing faced by public tenants, private tenants and owner occupiers and commented:

An important concern about the introduction of the housing assistance scheme in this connection is that the assistance scheme could cause a serious increase in the price of standard housing because of a very sluggish response of housing supply, causing the assistance to be diverted to landlords rather than low income households. This was one of the concerns which led to the housing allowance supply experiments in the United States....

Another important reason why there were not large housing price increases following the introduction of housing allowances in the American experiments,
and also a possible shortcoming of this restricted type of housing assistance programme, is that only about 40 percent of the eligible households actually participated in the programme, because of the minimum standards requirement. Many low income families appear to have found that the minimum standards requirement forced them to allocate more of their income to housing than they normally would, and the housing assistance payment was insufficient to compensate for this distortion in their choices.

Kemp (1994, p. 35) in his article examining the British review of housing allowances stated: ‘…Income related housing allowances have apparently not, by themselves, been sufficient to induce an adequate supply of low income rental housing…’

There are therefore compelling arguments that place considerable doubt on the allocative efficiency of the private rental market in Australia and similar countries. This raises substantial questions about the long term efficiency of Rent Assistance, by itself, as a mechanism to provide affordable housing.

**The Effectiveness of Rent Assistance**

The objectives of Rent Assistance are outlined as follows:

Rent Assistance is provided as a component of the core social security programs for the retired, the unemployed, families with children, people with disabilities and the sick and people in special circumstances. Accordingly, Rent Assistance is designed to support the primary objectives of these programs -- adequate income support for clients and their dependents -- by providing supplementary assistance to meet the additional cost of private rental housing.

Unlike rent rebates in public housing, Rent Assistance does not function as a direct subsidy on the rents of private tenants. While the amount of the Rent Assistance is related to the level of rent and assists people to meet the costs of private rental accommodation, the payment is delivered as a component of pension or allowance (Karmel, 1988, p. 161).

A useful means of examining the effectiveness of the Program is to identify the proportion of gross income before and after Rent Assistance which is paid by recipients in rent, and to identify where and how Rent Assistance alleviates housing stress. To carry out this analysis we have obtained Rent Assistance entitlements for the June quarter 1994 and 2000, and the median rents for different types of dwellings in Melbourne and Sydney Local Government Areas over the same period. *The key question is* – does RA move substantial proportions of tenants in housing stress below the affordability benchmark? That is, does receipt of rent assistance change the situation of tenants so that, after RA, they now pay less than 30 per cent of their household incomes in rent?

**Rent Assistance Criteria**

Set out below are the Rent Assistance Criteria and maximum Rent Assistance payable in June 1994 and June 2000. June 1994 was chosen as the commencing date because it was shortly after major changes and increases in the entitlements under the Rent Assistance Program in 1993.
Table 6: Rent Assistance Criteria: June 1994 and June 2000

<table>
<thead>
<tr>
<th>Family Type</th>
<th>Maximum Fortnightly Rent Assistance</th>
<th>Minimum Fortnightly Rent</th>
<th>Minimum Fortnightly Rent For Maximum Rent Assistance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single, no children</td>
<td>68.40</td>
<td>77.20</td>
<td>61.20</td>
</tr>
<tr>
<td>Single, 1 or 2 children¹</td>
<td>75.20</td>
<td>90.20</td>
<td>81.40</td>
</tr>
<tr>
<td>Single, 3 or more children</td>
<td>85.80</td>
<td>102.00</td>
<td>81.40</td>
</tr>
<tr>
<td>Couple, no children</td>
<td>64.40</td>
<td>72.60</td>
<td>102.00</td>
</tr>
<tr>
<td>Couple, 1 or 2 children</td>
<td>75.20</td>
<td>90.20</td>
<td>122.0</td>
</tr>
<tr>
<td>Couple, 3 or more children</td>
<td>85.80</td>
<td>102.00</td>
<td>122.0</td>
</tr>
</tbody>
</table>


For the purposes of the analysis we assumed maximum incomes from all pension and benefit sources, additional income up to the ‘Income Free’ threshold (i.e. including the maximum fortnightly income that could be earned before pension and benefit entitlements would be affected) and then added the maximum Rent Assistance entitlements.

Table 7 sets out the details.

Median rents¹⁰ for 1 and 2 bedroom flats, and 2 and 3 bedroom houses for all Melbourne and Sydney Local Government Authority areas were then used to calculate the before and after Rent Assistance proportion of income being absorbed by rent.

That is, for each household type, the proportion of income required to rent the average (median rent) dwelling was calculated for one and two bedroom flats and houses in each LGA of the two cities. This proportion is defined as the ratio of median rent to income inclusive of RA. In other words, RA is treated as an income supplement not a tied housing allowance.

Table 7: Maximum Fortnightly Income: All Pension and Benefit Recipients: Before and After Rent Assistance: 1994 and 2000

<table>
<thead>
<tr>
<th>Family Type</th>
<th>Max Pens. &amp; Benefit Income: All Sources</th>
<th>'Income Free' Amount</th>
<th>Max. Income Before Rent Assistance</th>
<th>Max. Income After Rent Assistance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single, no children</td>
<td>323.3</td>
<td>377.4</td>
<td>88.0</td>
<td>102.0</td>
</tr>
<tr>
<td>Single, 1 or 2 children under 13-15</td>
<td>534.1</td>
<td>679.2</td>
<td>136.0</td>
<td>150.0</td>
</tr>
<tr>
<td>Single, 3 or more children under 13-15</td>
<td>624.7</td>
<td>811.4</td>
<td>160.0</td>
<td>174.0</td>
</tr>
<tr>
<td>Couple, no children</td>
<td>535.8</td>
<td>626.4</td>
<td>152.0</td>
<td>180.0</td>
</tr>
<tr>
<td>Couple, 1 or 2 children under 13-15</td>
<td>717.0</td>
<td>890.8</td>
<td>200.0</td>
<td>228.0</td>
</tr>
</tbody>
</table>

¹⁰ NSW DEPARTMENT OF HOUSING, OFFICE OF HOUSING VICTORIA, 1994 and 2000, Rent and Rental Reports
Results of Analysis

Table 8 summarises, for Melbourne and Sydney, the proportion of LGAs in each city that each household type could afford to rent within, for each type of dwelling noted. Thus, for example, it is evident that in both cities, single person households could not afford to rent in any metropolitan LGA, in either year; put another way, to rent anywhere would require singles to pay more than 30 per cent of their incomes to rent any type of median priced dwelling, even if they receive their full RA entitlement. Couples with 1 or 2 children, on the other hand, could afford to rent, say, a two bedroom flat in 51 per cent of Melbourne LGAs in 1994, though this figure had fallen to 39 per cent by 2000.

Table 8: Rent Assistance: Proportion of Metropolitan Locations Where Recipients Can Rent Without Being In Housing Stress: Before and After Rent Assistance: 1994 and 2000

<table>
<thead>
<tr>
<th>Family Type</th>
<th>1 Bedroom Flats</th>
<th>2 Bedroom Flats</th>
<th>2 Bed. Houses</th>
<th>3 Bed. Houses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Melbourne</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Single 94</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Single 20</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Single 1 or 2 Child 94</td>
<td>90%</td>
<td>100%</td>
<td>10%</td>
<td>16%</td>
</tr>
<tr>
<td>Single 1 or 2 Child 20</td>
<td>32%</td>
<td>48%</td>
<td>16%</td>
<td>Nil</td>
</tr>
<tr>
<td>Couple No Child 94</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Couple No Child 20</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Couple 1 or 2 Child 94</td>
<td>100%</td>
<td>100%</td>
<td>-</td>
<td>77%</td>
</tr>
<tr>
<td>Couple 1 or 2 Child 20</td>
<td>58%</td>
<td>61%</td>
<td>3%</td>
<td>55%</td>
</tr>
<tr>
<td>Sydney</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Single 94</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Single 20</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
</tbody>
</table>

Source: Unpublished Data: Commonwealth Department Of Family and Childrens Services, April 2001
<table>
<thead>
<tr>
<th></th>
<th>Single 1 or 2 Child 94</th>
<th>Single 1 or 2 Child 20</th>
<th>Couple No Child 94</th>
<th>Couple No Child 20</th>
<th>Couple 1 or 2 Child 94</th>
<th>Couple 1 or 2 Child 20</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>10% 22% 12% Nil 10%</td>
<td>16% 20% 4% Nil Nil</td>
<td>16% 20% 4% Nil</td>
<td>14% 25% 11% Nil</td>
<td>49% 57% 8% 22% 26%</td>
<td>34% 53% 19% 18% 25%</td>
</tr>
<tr>
<td></td>
<td>Nil 4% 4% Nil Nil Nil</td>
<td>Nil 4% 4% Nil Nil Nil</td>
<td>4% 20% 16% Nil</td>
<td>4% 20% 16% Nil 2%</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>10% Nil Nil Nil Nil</td>
<td>10% Nil Nil Nil Nil</td>
<td>22% 26% 4% 4% 20%</td>
<td>16% Nil 2% 2%</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Nil Nil Nil Nil Nil</td>
<td>Nil Nil Nil Nil Nil</td>
<td>4% 16% 6% 22% 16%</td>
<td>Nil Nil 2% 2%</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Nil Nil Nil Nil Nil</td>
<td>Nil Nil Nil Nil Nil</td>
<td>4% 16% 6% 22% 16%</td>
<td>Nil Nil 2% 2%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

To summarize:

- for single persons and couples without children eligible to receive Rent Assistance there is almost no type of rental dwelling that is affordable anywhere, either in Melbourne or Sydney;

- Rent Assistance provides no substantial alleviation of housing stress with these family types;

- the locations where these households will not experience housing stress has declined significantly since 1994, and Rent Assistance is effective in providing locational choices in a much smaller range of LGA’s in 2000 than in 1994;

- for single persons with one or two children and eligible to receive Rent Assistance, only 1 or 2 bedroom flats are affordable in 48% and 19% of Melbourne LGA’s in 2000, and the number of appropriate locations declined by approximately 50% between 1994 and 2000, for this group. In Sydney only one bedroom flats are affordable in just 20% of locations (i.e. all other dwelling types are not affordable by this group in any LGA); and, again, the Rent Assistance program was far less effective in widening choice in 2000 than in 1994;

- couples with 1 or 2 children and eligible to receive Rent Assistance have a wider range of locational and dwelling choices than any other group, but only where this group is renting three bedroom housing is Rent Assistance providing greater choices than in 1994;

- as a whole, affordability for pension and benefit recipients has rapidly declined between 1994 and 2000, and Rent Assistance was much less effective in broadening dwelling and locational choices in 2000 than in 1994. Whatever level of effectiveness achieved has been and remains largely confined to family types with children present.

In other words, the Rent Assistance program is relatively ineffective in providing either a wider range of dwelling or locational choices for the large majority of recipients in either Melbourne or Sydney. The limited impact of the program on housing affordability has also apparently declined substantially over the second half of the 1990s.
The Equity of Rent Assistance

There are two-types of equity generally considered in the assessment and development of public policy:

- **horizontal equity**, which can be described as the objective that people in equal positions should be treated equally. However, to operationalise this concept, ‘equal position’ must be defined. This definition has generally been based on some observable index of ability to pay, such as income, expenditure or wealth; and

- **vertical equity**, which also relates to an individual’s ability to pay but in this case can be described as the objective that people should pay according to their capacity.

Horizontal equity demands that those on similar incomes pay the same. Adherence to horizontal equity implies that individuals and households with the same incomes should receive the same amount of cash support or housing benefit.

As regards horizontal equity the Rent Assistance Program is deficient in two important respects.

- Singles, and couples without children, fully employed in a low wage context, renting in the private sector, and not receiving any pension or benefit, do not receive any Rent Assistance. By contrast, those pension and benefit recipients enjoying identical incomes to this low wage group but with some part of that income accruing from a pension or benefit will, however, receive full Rent Assistance entitlements. Thus, the primary eligibility criteria for the receipt of Rent Assistance is not incomes and privately renting, but being a pension and benefit recipient and privately renting. In this respect the Program violates horizontal equity principles.

- for the same types of individuals and households enjoying the same incomes, the proportionate value of the housing benefit conferred varies widely across Australia. For a given type of recipient, the maximum amount of Rent Assistance paid and the maximum rent paid cut off level is the same whether it be Sydney or Alice Springs or East Gippsland in regional Victoria. The amount of housing services that can be purchased varies dramatically because of the very different housing cost structures in these cities and regions.

Cost and Risk

Graph 30 sets out for Sydney, the annual percentage change in selected variables that affect housing costs and housing assistance subsidies in any given housing sub-market.
affected by market fluctuations and crises. Homburg & Pomeroy (1996) The ranges for the key variables are:

- CPI, -0.28% to 11.39%;
- House Prices, -0.7% to 43.3%;
- Rents, -16.3% to 41.3%;
- AWE, -0.5% to 11.7%;
- Unemployment Rate, -23.2% to 47.4%;
- 90 Day Bank Bills, -5.99% to 19.75%;
- 10 Year Commonwealth Bonds, -6.7% to 15%; and
- Bank Variable Rate Home Loans, -21.43% to 18.92%.

Gross rents have the greatest range and therefore volatility of all variables. This suggests that in Sydney, at least, a program directed at subsidising rents may carry the greatest financial risk to the Commonwealth. Of course, further research throughout Australia would be necessary to confirm whether this finding could be generalised across all capital cities.

Yates and Whitehead (1998, p. 420) allude to these and similar risks:

Kleinman (1995), for example, has suggested that the move to greater reliance on personal subsidies has resulted in a housing system which has become more closely report concerns that increased reliance on the private sector in fact, exacerbated market fluctuations. Priemus (1996) has related this to the loss of the stabilising role of supply-side subsidies. These concerns highlight the fact that differences in the timing of discretionary compared with as-of-right subsidies can affect outcomes.
In many countries however, greater reliance on private sector finance has increased the cost of housing allowances (Homburg & Pomeroy, 1996; Turner et al., 1996). This can be attributed to the increased uncertainty and hence risks associated with the continuity of the demand-side subsidies needed to ensure funding mechanisms are viable. In some countries these risks have been managed by the development of guaranteed or capitalised intermediaries. In others, however, they remain.

Yates and Whitehead (ibid., p. 420) go on to point out:

This results in increased risk to the recipient, who has no guarantee that housing will continue to remain affordable; to funders, who therefore have no guarantee that repayments will continue; and to governments potentially faced with ever expanding housing allowance claims. In addition, there is no guarantee that risk averse private suppliers will respond in the same way as social landlords to government incentives.

The risks to the government of expanding demands on demand-side subsidies have led some authors to suggest rent subsidy programmes are more vulnerable to cutbacks (Angel, 1992). The benefits of personal subsidies can disappear overnight whereas it takes longer to dismantle the cumulative effect of subsidised stock.

Conclusions

Clearly, there are serious issues associated with the efficiency, effectiveness, equity and riskiness of the Rent Assistance program, such that it would be unwise to concentrate all assistance provision through this one mechanism.

The program, it has been demonstrated above, has very limited effectiveness in both Melbourne and Sydney and due to the capping of the assistance criteria that limited effectiveness is declining. To have maintained the effectiveness of the Program at 1994 levels would have required a significant increase in the rent cut-off levels and maximum amount of Rent Assistance payable. This in turn would have meant a very substantial increase in funding for the Program that would have to be met entirely from Commonwealth funds.

Extra government funding will indeed be required to deal with the increasing problems of housing affordability in Australia, some of which could usefully be committed to raising the effectiveness of the rent assistance program. However, in order to stretch available government housing subsidy funds further, it would be wise for government to consider ways of leveraging some of those public funds with private funds, as well as expanding rent assistance through the income support system and capital provision through the CSHA. In the light of the various financial and operating risks facing housing authorities, a mixed strategy of delivering the necessary expanding pool of housing assistance through these three main channels – RA, CSHA and leveraged private investment – is most likely to maximise the overall effectiveness of policy on housing affordability and minimise the long term subsidy costs per household assisted. (Stages 2 and 3 of this project develop effective private leveraging options intended to complement the established housing assistance approaches.)

Two further conclusions can be advanced, based on the analysis in this section.

First, the Rent Assistance program does not comply with the principals of horizontal equity.

Second, it is possible that the financial risks associated with the program are more significant than with the alternative supply side option or a mixed demand side-supply side strategy that also includes a leveraged private investment component.
3. The Changing Policy Climate

The barriers and challenges to encouraging greater institutional investment in affordable housing, discussed above, must be seen in the wider context of changes on-going in housing policy, taxation reform and the structure of Australia’s capital market.

3.1 Housing Policy

The current policy climate, characterised by significant capital and revenue constraints, has made the State Housing Authorities potentially open to new approaches to asset management which would leverage resources from the private sector. The key issues remain those to do with risk allocation, subsidy policy and political will.

The 1990s was a period of significant debate and change in housing policy in Australia. Housing has been caught up in the general move towards market-focused, neo-liberal policy reform, apparent in most of the Anglo-democracies over that period. Yates (1997, p. 266) has commented:

Because of the changes which are taking place, the 1990s can be regarded as representing a watershed in relation to federal housing policies in Australia. In the immediate post-war period through to the 1980s, Australia’s housing system was dominated by tenure-based policies which were directed towards home ownership and the provision of public housing with private tenants virtually being excluded from housing assistance of any form…. In the 1990s, however, we have seen, or are about to see, an apparent U-turn in federal housing policies with the elimination of explicit home ownership policies, the withdrawal of the Commonwealth from direct involvement in public housing funding and a rapid expansion of rental assistance for private tenants.

In fact, at the time Yates was writing, the Commonwealth pulled back from the major reforms that would have meant the replacement of capital subsides for public housing in favour of demand-side subsidies in the form of rent assistance paid to both public and private tenants. The 1996 Commonwealth State Housing Agreement (CSHA), originally intended as an interim arrangement, was eventually extended to 2003. Under this agreement the Commonwealth undertook to continue to maintain capital grants to the SHAs, with state government matching, albeit at a falling real value, pending renegotiations of future arrangements to be commenced in 2001.11 However, the general shift away from supply-side to demand-side subsidies is apparent in the funding contributions of the Commonwealth over the past 10 or 15 years (see Figure 1).

The 1996 CSHA enshrined a number of changes from earlier agreements. The 1984 CSHA had clearly specified as a major objective the expansion of the public housing stock managed by the SHAs. A commitment was also made to providing housing assistance to all those in need as a way of solving existing housing-related poverty. Both the 1984 and 1989 CSHAs limited the extent to which CSHA funds could be directed towards financing owner occupation, in order to

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11 The 1989 CSHA had converted all Commonwealth funds committed under the agreement from long term loans to grants. In fact, most Commonwealth funding supplied through the agreement had been in the form of grants since the mid-1980s. The 1989 agreement formalised this position.
give precedence to the aim of building up the public rental stock. The States were encouraged
to access private funds to finance their home ownership programs, which most did, with adverse
consequences for some in the early 1990s, notably in N.S.W. As a consequence annual
additions to the public rental stock ran at about 10,000 to 15,000 nationally during the 1980s.

The 1996 CSHA removed the objective of expanding public housing, and also removed any
mention of providing levels of assistance to meet all housing-related needs. There was more
emphasis on providing assistance at agreed levels and delivering subsidies in a way that would
enhance horizontal equity, the like treatment of people in similar circumstances regardless of
tenure. More accurately, this goal reflected the desire to treat all tenants, public and private, on
an equal footing. Owner occupiers would continue to benefit from taxation relief on capital gains
and imputed rent. The 1996 agreement also targeted the homeless and Aboriginal and Torres
Strait Islanders as groups with particular and pressing needs for assistance. This agreement
freed up the earlier constraints on SHAs moving CSHA funds out of their public rental accounts
to finance any Commonwealth allowable activity, including unrestricted funding of rental rebates
and stock renovation. As a consequence of this change, allied to the falling real value of annual
capital grants, a rising rental rebate bill and ballooning maintenance and upgrade costs, the
annual additions to the public stock have fallen to less than 5,000 in the last few years. This
constraint on the public stock has been reinforced by relaxation of the terms on which public
housing is sold. The proportion of sales to additions rose from less than 10 per cent in the mid-
1980s to around 30 per cent in the mid-1990s.\footnote{The 1996 agreement also moved some way to identifying and separating Commonwealth roles and responsibilities in housing provision, introducing transparent monitoring and reporting relationships. Greater flexibility was also sought through introducing bilateral agreements between the Commonwealth and individual States and Territories.}

These policy changes have emerged in the context of a number of major Commonwealth
sponsored research programs and public inquiries. The Housing Policy Review (1988-89)
reinforced the concern with the high incidence of housing stress in the private rental sector, underlining the growing concern about horizontal inequity between public and private renters but cast doubt on the capacity of demand-side subsidies alone to remedy the problem. The National Housing Strategy (NHS) canvassed a range of options designed to extend housing affordability, access and appropriateness. It concluded that about 90 per cent of low income private tenants were paying in excess of 25 per cent of household incomes in rent in the early 1990s. Policies approaches were suggested that aimed at reducing that level of housing stress, including a mix of demand-side and supply-side subsidies, the encouragement of public-private partnerships, and the creation of more efficient urban forms.

The (then) Industry Commission brought down its report on public housing in 1993. A main conclusion was that public housing offered the most cost effective way of delivering housing assistance in the long term, and was in that sense preferable to approaches relying mainly on rent assistance, headleasing and the like. However the Commission also pointed to the need to clarify and order the housing objectives of all levels of government, increase the transparency of subsidy arrangements, establish clear benchmarks against which performance is monitored and define and separate the appropriate roles of the Commonwealth and States and Territories.

In 1990 a Special Premiers Conference was convened to put housing assistance on the agenda of microeconomic reform, in line with the general program of collaboration between the levels of government that culminated in 1992 with the formation of the Council of Australian Governments (COAG). In 1994 COAG requested Housing Ministers to report on housing policy reforms that would address the issues raised by the Industry Commission report. COAG considered the Ministers’ response in 1995 and established the following four principles that should guide future housing assistance policy:

1. Clearer delineation of Commonwealth and State/Territory roles, with the Commonwealth assuming primary responsibilities for income support and the States and Territories bearing the responsibility for public housing provision and management.

2. A national needs assessment that would ensure that the level of assistance would be determined on a consistent basis across all jurisdictions.

3. Output rather than input targets to be established and monitored. This suggested a regime that would focus on actual results rather than intended outcomes.

4. Implementation of a charter of resident rights.

This process was influential in guiding the negotiations responsible for the 1996 CSHA and in subsequent developments. Bilateral agreements specifying output targets and agreed benchmarks for performance have, as noted above, been instituted between the Commonwealth and States/Territories. A number of States have moved towards tighter targeting of available public housing dwellings towards groups deemed to be in greatest need. For example, in 1997 Victoria moved to make eligibility for public housing the same as eligibility for social security benefits and pensions. Victoria subsequently began raising rents for existing public tenants from 20 per cent to 23 per cent of assessed income and 25 per cent for new public tenants.

Over the past few years the SHAs have sought to rationalise and consolidate their activities in both public renting and support for home ownership, generally in the context of a slowly declining level of activities, in line with the falling real value of Commonwealth and State resource commitments to this policy field and some uncertainty as to the longer term future of the CSHA. Conversely, the Commonwealth’s fiscal commitment to rent assistance has continued to grow in total dollar terms, as Figure 1 shows. A number of SHAs are also having to battle with fiscal and management problems posed by a rapidly obsolescing public stock and therefore to show interest in possible approaches to area regeneration, particularly in relation to their large estates.
3.2 Taxation Reform

Taxation in its various forms is clearly a major factor in investor decisions about where to invest and in what portfolio mixes. As the earlier discussion clearly demonstrated, some countries use subsidies delivered through the taxation system as a prominent means of encouraging private investment in affordable housing. Debate about Australia’s tax system has been underway since the early 1980s, culminating in the last few years in a major program of reform.

Housing investment is necessarily impacted by the general changes that have been implemented, especially to the capital gains tax. For example, the changes to CGT in the way depreciation on fixed assets is calculated, introduced in May 1997, effectively reduced returns on assets like housing by comparison to investments with a smaller or zero proportion of return dependent on the changing capital value of the underlying asset. The changes to CGT in September 1999 effectively cut the maximum rate for individuals to 24.25 per cent (half the nominal gain at the top marginal tax rate) and 30 per cent for companies (the company tax rate applied to the full nominal gain). Registered charities continue to be exempt. This may provide some incentive for high income individuals to invest more in assets like housing that generate a significant proportion of returns in capital growth. But, in general, social housing will not necessarily be preferred over other appreciating property or non-property assets.

The introduction of the New Tax System, including the GST, in July 2000 also has implications for housing investment. Investment in rental dwellings is input taxed under the GST, which means that although rents are exempt, input credits cannot be claimed by most investors on construction, maintenance, management and renovation of the asset and GST is payable on the sale of new and substantially renovated homes. However, charitable social housing providers registered for the GST can claim input credits. This may offer some scope for joint ventures between charitable providers and private investors utilising the GST status of the former.

A fuller treatment of taxation issues in the context of this study is put off until stage 2 of the project. Recommendations of the second stage of the Ralph Report on business taxation reform will be publicly released on 7 December. Preliminary advice to the researchers from Clayton Utz recommends waiting until this information is available before seeking detailed advice on the implications of recent changes in taxation regimes for investment in affordable housing. The researchers will be following this matter up with Clayton Utz in a meeting planned in Sydney for the 19 December.

3.3 The Growth of Superannuation Savings

One of the major developments in the Australian capital market over the past decade and a half has been the extension of minimum superannuation coverage to virtually all workers. The total volume of superannuation savings in Australia stood at about $450 billion (Monash Sustainability Enterprises, 2000, p. 8) in early 2000. This figure is expected to reach $2 trillion by 2010 (Clark et al., 1996). This, in short, is where ‘the weight of money is.’ If private investment is to flow into affordable housing then the superannuation funds will be major players.

This development has been the result of deliberate government policy, dating from the mid-1980s, designed to relieve future governments and taxpayers of the otherwise rapidly rising burden of the age pension in an aging society. In 1985 the ACTU accepted a 3 per cent employer superannuation contribution in lieu of a pay rise for workers. This agreement was ratified through the Conciliation and Arbitration Commission and progressively implemented industry to industry and occupation to occupation. By the end of the decade around 70 per cent of the workforce were effectively covered by some sort of superannuation arrangement. In the
1991-92 Federal Budget the government signalled that it would be bringing down legislation to introduce universal – i.e. compulsory – superannuation coverage for all Australian workers. The Superannuation Guarantee (Administration) Bill was passed in April 1992, establishing the Superannuation Guarantee Scheme (SGS). This called for employers to contribute a minimum of 5 per cent of the normal remuneration of workers to an approved fund, rising to 9 per cent over the next nine years.

The next critical step in the evolution of a national superannuation system came in the wake of the Fitzgerald report on national savings. This report pointed to the relatively low rate of national savings in Australia, which posed future problems both because of the constraints placed on economic growth and the growing unfunded liability for age pensions and other retirement needs. Among the Fitzgerald recommendations was for the introduction of compulsory employee contributions to superannuation, in addition to the mandated employer contributions. This recommendation was accepted in the last Labor Budget of 1995-96. Employee contributions of 3 per cent were to be phased in matched by a 3 per cent contribution by government, the latter in lieu of previously promised income tax cuts.

The Coalition inherited the SGS on assuming government in April 1996. It has, broadly, maintained a bipartisan approach to this area. The current government did, however, introduce two significant changes. First, banks and some other financial institutions have been allowed to compete for this growing pool of savings by offering special retirement savings accounts designed to preserve benefits until after the saver leaves the workforce. Second, an income tax surcharge has been imposed on the future tax deductible contributions of higher income earners (including contributions made through salary sacrifice arrangements). Interestingly, although flirting with it during the 1996 election campaign, the Coalition in power has rejected the proposal – pushed strongly by housing industry groups – that workers be able to tap their superannuation savings for a deposit on home purchase.

The other important development during the 1990s, in view of the focus of this project, is the growth of fund member choice. The Superannuation Industry (Supervision) Bill, 1993 effectively allows fund members – i.e. savers -- to be involved in decisions about how their savings are invested. This applies not only to accumulation funds but also to defined benefit funds, such as many of the government employee schemes. Since then an increasing number of funds and fund managers in Australia have begun offering products incorporating member choice. This now places extra responsibilities on fund trustees to provide members with adequate information on which to make informed choices. It also opens the door to large-scale ethical investing, as argued in section 4.3, below.

In a definitive study of the rise and role of superannuation or pension funds in the Anglo-Democracies, including Australia, Gordon Clark (2000) argues that ‘alternative investment product’ or AIPs, incorporating what have earlier been referred to as economically targeted investments and socially responsible investing, potentially provide a rapidly growing source of funds for socially important purposes, like urban infrastructure, venture capital and housing. Most AIPs have, as Clark stresses, been delivered in one-off packages, entailing very high transaction costs. Because they are one-off trustees face problems of ‘veracity’, how to gain sufficient independent and reliable information on which to judge the real – as opposed to claimed – characteristics of the product on offer. What is required, Clark (2000) argues, is the intervention of second order financial intermediaries, which are:

...institutional mechanisms for parcelling or pooling together diverse sources of funds, so as to take advantage of diversification ('the law of large numbers') on a cost-effective basis (the virtues of 'larger scale'). These intermediaries are functionally located between pension funds and financial services markets offering expertise in project-based investment management and management of the flow of funds.
These intermediaries are needed in order reduce the ‘opacity’ of investment products like AIPs, to share or allocate risks among the various interests involved and to guarantee a degree of liquidity or an ‘exit option’ for pension funds wishing to sell their stake. Clark identifies a number of forms that such intermediaries could assume. The first and least radical form is for established funds managers to modify existing products incorporating particular features like the screening out of specific activities. This, along with the next type discussed below, is the form of AIP most familiar in the ethical investing world.

An alternative is to develop new specific purpose mutual funds with a defined investment charter. Thus, in the United States the AFL-CIO Housing and Building Investment Trusts have been established to direct the savings of workers into construction projects throughout the country. HITs and BITs, as they are known, rely on a government mortgage guarantee as part of their risk allocation structure. In Australia in the mid-1990s, the (then) National Mutual insurance company teemed with a number of ACTU industry superannuation funds to establish the Superannuation Members Home Loans Scheme as a vehicle for those funds to advance mortgage loans for home purchase to their members at highly competitive rates. This vehicle is owned by National Mutual/AXA and issues mortgaged backed securities by pooling the loans of individual fund members and selling the securities back to the funds.

Clark argues that AIPs delivered in the forms just described tend to depend on existing financial products. He also points to more innovative organisational forms of intermediation that manage very large volumes of funds allowing new AIPs to be developed, say with a focus on housing, on the margins of highly diversified portfolios. This effectively reduces the design costs of the new products by trading on the ‘sunk costs’ of the established organisation. Such organisations are able to hold the AIPs for the longer term, in line with the liability profiles of investing funds, unlike smaller less diversified organisations (Clark, 2000, p.197). An example of an intermediary playing this role is New York City’s Bureau of Asset Management (BAM) which provides investment services to five of the City’s largest pension plans. An Australian example is offered by IFS, set up by the ACTU industry superannuation funds for similar purposes. Organisations of this type and mission are well placed to broker new AIPs for the funds, although – as Clark stresses – fund trustee conservatism raises barriers to the acceptance of new products of any kind.
4 Barriers to Private Sector and Non-Government Finance for Affordable Housing

4.1 Introduction

Increasing housing stress is, somewhat paradoxically, emerging during a period that has witnessed a pronounced upward trend in housing finance for owner-occupation. Since deregulation of Australia’s financial system in the early 1980s, primary and (in the 1990s) secondary mortgage markets have grown rapidly, fueled by two major property booms. However, access to mortgage finance is steeply skewed towards re-financing existing, rather than new, dwellings and in favour of those who are well placed in the ‘new knowledge economy’ (Berry, 1999; 2000a). Increasing affordability problems for aspiring low-to-moderate income home owners place further demands on the limited stock of rental accommodation. Given that public and community housing agencies are not able, in the current policy environment, to significantly expand their stocks of affordable housing, these demands fall squarely on the private rental market.

The key question then is – to what extent is the private rental sector able to meet the challenge? The answer turns, in part, on the current pattern and drivers of private investment in the rental sector. After outlining this situation the report considers the marginal role of institutional investors in rental provision to date, summarizing a number of cases of limited institutional involvement in Australia by comparison to more active interventions in other OECD countries. The report then focuses on the effective barriers to greater institutional investment in Australia before outlining the possible range of alternative approaches for overcoming those barriers. The final chapter sketches key changes in the public policy environment over the past decade that have impacted on housing outcomes.

4.2 Investment in the Provision of Rental Housing

The structure of private rental investment in Australia has been well described by Yates (1996), Beer (1999) and Berry (2000b), based on surveys of rental investors carried out by the Australian Bureau of Statistics (1994, 1998). The key findings of this work are as follows:

- over 60 per cent of private rented dwellings are owned by individuals, with most of the remainder of the stock owned by partnerships and small companies;
- 76 per cent of individual landlord-investors own only one rental property; a further 16 per cent own two;
- 75 per cent of landlord-investors are also home owners, higher than the Australian average;
- the median (gross) income of landlord-investors (in 1997) was in excess of $1000 per week, twice the national average, though this high average masks the very significant range of incomes from low to very high for this group;
- landlord-investors are primarily concerned to ensure a long term, secure investment outcome. A series of other motivations (e.g. capital gains or negative gearing) are relevant but less pressing (see Figure 2) Interpreting these responses is difficult; for some landlord-investors the category ‘long term investment’ may act as a catch-all for other financial goals;
- there is a significance incidence of what Yates (1996) has termed ‘accidental landlordism’. For example, about one-quarter of landlord-investors are renting out the house they previously
Figure 2: Reasons for Investing in Rental Property, June 1997

* the total number of investor income units was 584,200. The numbers in the graph add to more than this total, since respondents were asked to state all reasons considered for investment.
Source: ABS, Household Investors in Rental Dwellings, Australia, 1997, p.17, (Catalogue No. 8711.0)
Table 9: Rates of Return to Rental Investors by Income of Investor, June 1997

<table>
<thead>
<tr>
<th>Gross Weekly income quintile group&lt;sup&gt;(a)&lt;/sup&gt;</th>
<th>Lowest</th>
<th>Second</th>
<th>Third</th>
<th>Fourth</th>
<th>Highest</th>
<th>Not Stated</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross rate of return&lt;sup&gt;(b)&lt;/sup&gt;</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>less than 5%</td>
<td>8.9</td>
<td>*</td>
<td>9.7</td>
<td>9.4</td>
<td>7.2</td>
<td>8.6</td>
<td>8.3</td>
</tr>
<tr>
<td>5%</td>
<td>9.5</td>
<td>13.8</td>
<td>14.5</td>
<td>12.2</td>
<td>16.8</td>
<td>12.7</td>
<td>13.2</td>
</tr>
<tr>
<td>6%</td>
<td>16.4</td>
<td>22.1</td>
<td>18.4</td>
<td>19.9</td>
<td>32.4</td>
<td>18.4</td>
<td>21.1</td>
</tr>
<tr>
<td>7%</td>
<td>21.1</td>
<td>16.6</td>
<td>24.7</td>
<td>25.3</td>
<td>20.7</td>
<td>22.3</td>
<td>21.9</td>
</tr>
<tr>
<td>8% or more</td>
<td>36.7</td>
<td>37.7</td>
<td>28.4</td>
<td>30.6</td>
<td>20.2</td>
<td>25.1</td>
<td>29.3</td>
</tr>
<tr>
<td>unknown</td>
<td>7.6</td>
<td>*</td>
<td>*</td>
<td>*</td>
<td>*</td>
<td>12.9</td>
<td>6.3</td>
</tr>
<tr>
<td>Total</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

| Net annual return<sup>(c)</sup>                |        |        |       |        |         |            |       |
| Loss                                           | 26.2   | 32.3   | 42.9  | 42.0   | 41.8    | 32.6       | 35.9  |
| Break even                                     | 13.5   | 15.9   | 8.9   | 7.8    | 9.7     | 10.6       | 11.0  |
| Profit                                         | 39.1   | 32.2   | 30.2  | 26.2   | 23.6    | 26.5       | 29.4  |
| Not Stated                                     | 7.0    | 7.1    | 5.8   | 9.2    | 7.7     | 16.3       | 9.5   |
| Not Applicable<sup>(d)</sup>                   | 14.2   | 12.5   | 12.1  | 14.9   | 17.2    | 14.0       | 14.1  |
| Total                                          | 100.0  | 100.0  | 100.0 | 100.0  | 100.0   | 100.0      | 100.0 |

<sup>(a)</sup> For gross rate of return, includes income units with sole ownership of property, only (representing 83 per cent of total investor income units).

<sup>(b)</sup> Gross rate of return is defined as gross annual rent divided by the current value of the property.

<sup>(c)</sup> The net profit or loss, as reported by the respondent, made on the property after all related costs (including interest costs and depreciation) are deducted from rent, for the 1995-96 year.

<sup>(d)</sup> Respondents who acquired property after June 1996 were excluded.

Source: ABS, *Household Investors in Rental Dwellings, Australia, 1997*, p.17, (Catalogue No. 8711.0)
• lived in as owner-occupier, others had inherited their rental dwellings and were not necessarily long term landlords. Almost 7 per cent at the time of the 1997 survey were trying – unsuccessfully – to sell their rental dwellings;

• the financial rates of return reported varied very widely across the group (see Table 9). Eight per cent of investors reported gross rental yields under 5 per cent (p.a.) while almost 30 per cent achieved yields over 8 per cent;

• net returns (before tax) were similarly widely spread. More than a third of all landlord investors reported a loss on their rental operations for the 1995-96 year. Under 30 per cent reported a before-tax net profit;

• lower income investors were more likely to show a net profit, and higher income investors a loss, which may reflect the latter’s capacity to offset part of the loss on renting by negatively gearing (at high marginal income tax rates) against other income.

The overall picture of the private rental sector emerging is of a disparate and fragmented ‘cottage industry’, with low barriers to entry and frequent movement – of investors and dwellings – into and out of the sector but with a solid core of investors who are ‘there for the long haul’. This further suggests that not all investors in rental property will respond ‘rationally’ to market signals. For some, non-economic concerns with ‘bricks and mortar security’ or emotional attachment to their dwellings will override careful calculations of returns and costs. Substantial numbers of landlord-investors will earn less than full commercial rates of return on their rental investment. This factor will impact on the rent that can be charged in general and, therefore, limit the capacity of professional investors to achieve their (risk adjusted) target rates of return in this market.

The current pattern of rental investment in Australia is the historical outcome of our peculiar pattern of urban development. By comparison with European and even North American countries, Australian land and housing development has been strongly market-driven. Private capital has circulated freely in the built environment since the early Nineteenth Century, little hampered by direct government interventions or the existence of large religious or aristocratic land ownership. Town planning controls came late to Australia and have been largely responsive to rather than directive of property market forces (McLoughlin, 1992). Australia’s centralized system of wage fixation has recognized and fully incorporated market rent into the determination of wages for much of the Twentieth Century (Berry, 1999), underpinning demand for rental housing.

On the supply side the virtual absence of rent controls (except during wartime) has encouraged small investors to lock their savings into this sector, secure in the knowledge that future contingencies and cost increases can be met by raising rent to what the market will bear. Two further factors have encouraged small investors in this respect. First, landlord-tenant legislation enacted by the State governments has generally favoured landlords, allowing tenants strictly limited security of tenure. In practice this has meant that landlords have been able to regain possession of their dwellings at the end of short leases, to sell, re-let, re-develop or use themselves. Second, until the last 10 to 20 years, small investors had limited alternative investment options. In the highly regulated financial system that existed in Australia until the early 1980s, only large, professional and institutional investors had access to a range of investment opportunities. To some extent then, part of the accumulated investment of small investors in rental property was by default. Although much has changed in this respect as Australian financial markets have become less regulated and more flexible, inertial forces still lock small savings into the rental sector.

Taxation has impacted on rental investors in complex and diverse ways. Interest paid on loans to finance dwelling purchase and renovations has, in general, been deductible against the investor’s total income for income taxation purposes, unlike the situation in a number of other countries – for example, Britain. This may have influenced both the level of investment in this asset type and created so called ‘clientele effects’ – e.g. the tendency for higher income
investors (on the maximum marginal tax rate) to favour higher value properties in good locations which deliver capital gains rather than high rental yields (Wood and Watson, 1999). Capital gains tax has been a relatively late arrival in Australia and generally levied at rates that are effectively lower than for other income sources. Land taxes have also directly encouraged the fragmented, small scale structure of the industry; these taxes, levied by state government, exempt owner occupied and rental dwellings up to a threshold value. In effect, except in the very high value market segments (e.g. in parts of Sydney), the first rental dwelling or, perhaps two, avoid this form of taxation (Yates, 1996).

What is clear about the inherited pattern of rental investment in Australia, by comparison to a number of other advanced capitalist countries, is the virtual absence of institutional investors in this sector of the property market. This issue is taken up in the next section.

4.3 The Strictly Limited Role of Institutional Involvement in the Rental Sector

The predominant ‘petty landlord’ character of the Australian private rental housing sector is underscored by the absence of large corporate investors, especially the major financial institutions. With the exception of a few one-off schemes, some of which are outlined below, large investors continue to avoid this sector. Before looking selectively at overseas examples of much greater institutional investment in rental, especially affordable rental housing and the current barriers to similar approaches in Australia, this section will summarise some of the local attempts to enter this field.

From the mid-1980s onward some state housing authorities (SHAs) began to explore alternative ways of financing public housing provision, outside of or supplementary to the dominant policy vehicle, the Commonwealth State Housing Agreement (CSHA). This move was encouraged by a number of contemporary developments. First, the continuing trend towards ‘welfarisation’ of public housing saw non-working tenants dependent on government pensions and benefits effectively replace workers and their families in the public stock. This trend was driven both by changing economic and, especially, labour market conditions, and a policy shift towards market rents for public housing, the latter move dating from the Henderson Poverty Inquiry findings in the mid-1970s. Rising rental rebates for welfare tenants ate into the capacity of SHAs to fully maintain, still less significantly increase stock – hence, the search for supplementary sources of finance.

Second, increasingly tight public borrowing controls exercised through the Commonwealth Government-dominated Loan Council placed a severe capital constraint on state government investment. This occurred during a period in which there were increasing demands for a range of economic and social infrastructure facilities, including but going well beyond housing – e.g. roads, hospitals and airports. Alternative sources of finance that were ‘off-Budget’ and outside Loan Council limits were attractive to the States since this allowed scarce public borrowing resources to be directed to high priority uses elsewhere.

Third, far-reaching reforms and deregulation of the Australian financial system unleashed a wave of financial innovations and new products. Finance flowed strongly into the property sector in general, especially after the stock market collapse in 1987 and subsequent asset boom. Hence, potential new sources of finance and aggressive investment strategies of financial intermediaries opened up new possibilities for government agencies like the SHAs.

Fourth, the general political and ideological climate of the 1980s favoured a move towards ‘smaller government’ and greater reliance on private sector involvement in areas that were traditionally regarded as government-only provision or regulation. This policy view ranged from a commitment to public-private sector partnerships to full privatisation.
The main alternative approaches tried by the States are now outlined. Many of these approaches targeted institutional investors as sources of funds.

A. Debt Securitisation

During the 1980s some SHAs began to borrow through their Treasury corporations. FANMAC and NMMC were established by the NSW and Victorian governments (respectively) and issued housing bonds (both standard and indexed) to mainly institutional investors. This initial excursion into the secondary mortgage markets was short-lived as changes to the 1989 CSHA effectively prohibited SHA borrowing, with future Commonwealth loan funds under the Agreement converted to grants. Nevertheless, a deep secondary mortgage market reappeared and grew rapidly in the second half of the 1990s, driven by private investors and financial intermediaries. By 1997 one of the most active operators in the new market, Macquarie Bank, had facilitated the issue of more than $6 billion in mortgage-backed securities (through its PUMA vehicle). In that year more than $10 billion in mortgage backed securities (MBSs) were issued, including the first cross-border Eurobond transactions in which the large trading banks were involved (Standard and Poors, 1998).

The continued growth of this market demonstrates the willingness of institutions to invest in new areas, provided that appropriate products are developed that satisfy their basic investment requirements. It also indicates the eagerness of institutional investors, like the superannuation funds, to find new domestic fixed interest investment opportunities in a climate of cut-backs in government borrowing and a consequent shortage of government bonds.

B. Rental Housing Trusts

In 1985 the Commonwealth introduced a 4 per cent building allowance for income tax purposes on new rental housing, while removing negative gearing on all rental dwellings. Rental trusts were established in some states to acquire rental portfolios that would deliver a bundle of capital gains and taxation benefits to investors. In NSW the State Bank guaranteed rental trust investors a tax-free return of CPI plus 3 per cent through syndication of the housing assets and the sale of bonds. This structuring depended on the then current capital gains tax regime which exempted the inflation (i.e. CPI) component of gain in dwelling values from tax and on the 4 per cent building allowance. In fact, the Commonwealth had second thoughts on the latter issue. In 1987 it reversed its stance, reintroducing negative gearing and reducing the building allowance to its current level of 2.5 per cent. Even without this policy reversal, rental trusts as a viable vehicle for private investment were vulnerable to adverse taxation rulings, especially where government guarantees (as in the case of the State Bank example in NSW) were held to remove the residual risk of the investor.

In the trusts that were established there were no mechanisms in place guaranteeing that affordable rents would be charged or security of tenure protected. This short-lived experiment in alternative financing arrangements for rental housing offers two lessons. First, schemes or approaches that are strongly tax-driven are vulnerable to future changes in the tax rules or rulings (and investors know that). Second, without explicit mechanisms in place concerning who is to be housed and at what rents, the housing delivered may not be affordable for those in most need, or even if affordable, may not be occupied by those most in need.

13 Other difficulties emerged here. Funds raised through bond sales were directed into home purchase schemes for low income households, using low-start and indexed mortgages. As interest rates rose in the late 1980s financial stress intensified and the spectre of large-scale default appeared among this recent borrower group. Costly restructuring ensued, with further expansion of the schemes halted and subsequently run-down during the 1990s.
C. Joint Ventures

A number of States have developed partnerships with private investors and non-profit organizations to deliver housing services involving leasing, sale-and-leaseback, and corporate vehicle arrangements. In Victoria, for example, the Office of Housing’s head-leases dwellings and farms out management to selected community housing organizations. The Community Tenancy Scheme in New South Wales involves housing associations head-leasing from private landlords and on-renting to low income tenants. Similar schemes exist in Queensland and the A.C.T.

Sale-and-leaseback schemes were structured during the 1980s to pass taxation benefits related to depreciation/building allowances onto private investors in return for lower rent payments. This strategy was adopted by a number of State agencies that had traditionally owned expensive infrastructure assets like hospitals, railway rolling stock and police stations. The asset concerned was often ‘sold’ to the investor with a buy-back clause after a specified period of time. In effect, the investor was a lender carrying no risk on the asset’s residual value. The state agency was borrowing by stealth and the Commonwealth tax payer was effectively subsidizing the users of the asset in the state jurisdiction concerned.

However, the scope for SHAs to reduce costs and rents through such arrangements has been sharply curtailed by tightening Loan Council rules and taxation rulings. All finance leases and operating leases above a low threshold fall within Loan Council borrowing limits – i.e. they are treated as equivalent to public borrowing. Section 51AD and Division 16D of the Taxation Assessment Act require residual risk to be held by the investor claiming deductions for building allowances and depreciation on fittings and fixtures. This places limits on the type and extent of government involvement by way of equity or guarantee.

This leaves open the avenue of genuine investment joint ventures by government agencies. In general, this entails establishing a separate corporate vehicle or set of joint venture relationships with clear definition and distribution of roles and risks. To avoid falling afoul of Loan Council limits and taxation rulings such arrangements do not include buy-back or explicit (or implicit) government guarantees. The complexity and uncertainties surrounding this approach have severely constrained activity in this area. The financial design and other transaction costs entailed in getting such schemes started are high for one-off schemes. This imposes a scale constraint – schemes must be large enough to absorb high transaction costs. Box 1 summarises the Public Equity Partnership joint ventures between the New South Wales SHA and AMP Society (the so-called PEP1 and PEP2 schemes), prominent examples of this approach.

Cooperation has also developed between the SHAs and the non-profit sector. This often entails the creation of umbrella organisations to acquire dwellings on behalf of community housing organisations. For example, in Victoria, common equity rental cooperatives manage dwellings owned by a government vehicle, Common Equity Housing Inc., that has acquired a stock portfolio financed by a mixture of government equity and loans, and private retail loans. In South Australia, the South Australian Community Housing Authority raises loan finance through the state government’s finance authority to acquire dwellings which are managed by member housing associations. Similarly, Community Housing Canberra has been set up by the ACT Government to acquire and headlease dwellings to community sector providers.

The current Labor Government in Victoria was elected in 1999 with a commitment to invest an extra $90 million in affordable housing over the first three years of its term, and to do so in a way that would leverage maximum private investment into this sector. A target of 800 extra dwellings was proposed. In order to implement this aim the government established the Social Housing Innovations Program (SHIP) and carried out an extensive consultation process with existing community housing providers in the state, along with financiers, researchers and other interested groups. A report and recommendations, including longer and medium term visions, was
presented to the Housing Minister in late November 2000. This report is likely to be publicly released in December. To date, the only publicly available information is that about $11 million of the overall amount (of $94.5 million) has been added to other funds of the Office of Housing to fund new affordable housing projects with private and community sector partners; expressions of interest have been called and are due by January 2001. The remaining $83.5 million will subsequently be committed for the 2001-2003 period. Given the medium term timescale and limited funding, it is likely that the major emphasis will be on building capacity in the community housing sector, relying on well established organisations and attempting to moderately leverage outcomes both by recourse to conventional loan finance and through joint ventures with ethical investors. In the longer term, growing capacity in the sector may stimulate more interest by larger investors, especially the institutions.

**Box 1**

**Public Equity Partnership Schemes (PEP1 and PEP2)**

The PEP1 (1013 dwellings) and PEP2 (477 dwellings) schemes entered into between DOH and AMP have been in operation for 8 and 7 years respectively. Existing public housing dwelling units were purchased by the AMP Society (via a nominee company NSW Housing No.2 Pty Ltd) for leaseback to the DOH. Any vacancy after the first 12 months (PEP1) or 2 years (PEP2) must be let to private tenants and properties can be sold at any time after the completion of the the 10th year up to the end of the 21 year term.

The DOH is responsible for the overall management of the publicly let properties. However, a small number of properties which have been privately tenanted are managed by Stockland Property Management on behalf of DOH.

Under the conditions of the agreements, the DOH has certain financial obligations and rights:

- to pay a guaranteed pre-tax gross real rate of return to AMP. Inflation was assumed to be in the range of 4-14% (PEP1) and 0-15% (PEP2). The subsidy paid by the DOH is equal to the difference between actual rents received and the required rate of return. A tax saving to AMP accrues because any capital gains derived from the properties are subject to the same tax treatment as in a complying superannuation fund, that is, the cost base is indexed. This indexation and the capital indemnity which is treated by the ATO as sales proceeds effectively results in tax free capital gains to AMP. Therefore the gross rate of return is reduced by the extent of taxation deductions accruing from capital gains tax indexation and other direct income deductions.

- to receive from the transaction 75%(PEP1), and 66.6%(PEP2), of any real capital gains accruing from the properties. The financial model assumes real capital gains of 1%(PEP1), and 0(PEP2), and this automatically reduces the pre-tax gross real rate of return payable to AMP, as the transaction proceeds. To the extent that real capital gains exceed 1%, regular valuations ensure the model’s assumption is adjusted upwards (or downwards), to reflect reality, and 50% of 75%(PEP1), and 66.6%(PEP2) of the notional gain above 1% CPI is used to offset the pre-tax rate of return required, and the other 50% is notionally incorporated in a capital repayment reserve, as a hedge against future real capital falls.

- to pay from the capital repayment reserve or elsewhere a capital indemnity to AMP equivalent to the difference between net sale proceeds of a PEP property versus the original property price plus acquisition costs indexed to CPI+1% (PEP1) or CPI (PEP2). In the event that the net sales proceeds plus the capital repayment reserve exceed the required return the excess is returned to DOH; and

- to cover operating costs and other risks, DOH manages all properties and charges 0.5% of market value plus 2% of portfolio value for operating expenses (including maintenance).

Under PEP2 a special trust fund, the Rental Housing Assistance Fund (RHAF) was established by the Government to secure the financial obligations of the State to AMP. An insurance policy was effected to secure these obligations under PEP1.

In the transaction the taxation treatment obtained by AMP is assumed to be fixed for the course of its operation, that is CPI indexation and a tax rate of 15% plus other deductions so no tax risk applies. However changes to inflation can affect the extent of the capital gains tax indexation deduction, and therefore the extent to which the real gross rate of return is reduced by CGT indexation. Lower inflation and real capital gains reduces CGT indexation and hence increases subsidy payments. To the extent that the combined rents from public and private tenants does not achieve the required rate of return subsidies are paid.
During the late 1990s the N.S.W. Government established a Ministerial Taskforce on Affordable Housing which reported to the responsible Minister recommending more direct involvement by government at all levels in encouraging greater private-public sector collaboration in expanding the supply of affordable housing across the state. Subsequently, a two-year program of seed funding in the order of $2 million was implemented. The aim of the program – currently in progress – is to establish the viability of a range of affordable housing approaches through carefully selected, supported and monitored demonstration projects.

D. Town Planning Controls

Over the past 20 years governments in Australia have been attempting to stimulate the supply of affordable housing by controlling the form of housing and urban development. In 1982 the Commonwealth States and housing industry organizations established a joint venture for more affordable housing that produced the Australian Model Code for Residential Development (AMCORD). This code, its various up-dates and State manifestations sought to reduce housing costs by making land and housing development more efficient. The subsequent policy debates and developments gave rise to the term ‘urban consolidation’, a view of urban development that emphasized the need to increase average population and dwelling densities in cities and create a greater mix of densities there. Consolidation has been supported – and opposed – on a number of grounds, economic, social and environmental. However, it is clear that, to date, smaller lot sizes and more compact housing design has not produced significant affordability gains. This is probably because medium and higher density developments have tended to be located in inner and middle suburban locations where demand pressures push up the end price. In short, without complementary planning policies a simple move to greater densification is unlikely to result in affordable housing outcomes.

A number of planning mechanisms are relevant in this context, including conditional density bonuses, transferable development rights, ‘flexible’ development standards, ‘inclusionary zoning’, and linkage fees. The first three mechanisms are voluntary, negotiation-based approaches between developer and planning authorities, essentially ad-hoc and often small scale in application. Inclusionary zoning and linkage fees are mandatory mechanisms that are applied across the development sector; in these cases, the developer does not receive development consent unless specified conditions are met. Hence, ‘… inclusionary zoning may be simply defined as zoning provisions which require the mandatory provision of certain uses or facilities in identified new development proposals as a precondition before any approval may be granted by a planning authority’ (Williams, 2000, p. 29).

Williams (2000) summarises the recent efforts of New South Wales authorities to use inclusionary zoning in order to increase the stock of well located affordable housing. City West is a large urban redevelopment project in the Ultimo-Pyrmont area on the western entry to the Sydney CBD. This run down industrial and maritime area was mostly in public ownership. The aim of the City West Development Corporation established in the early 1990s, is to construct some 6 to 7 per cent of affordable housing in a total stock of 7,500 new dwellings, including 100 units of public housing. Legislative force was supplied through the Sydney Regional Environmental Plan No. 26 and amendments, which requires developers to either directly provide an appropriate proportion of affordable dwellings or make equivalent cash contributions that are pooled and invested in affordable units elsewhere in the overall development.

The second case described by Williams concerns Green Square in the City of South Sydney. The 275 hectare site is part of one of Sydney’s oldest industrial regions. Located on the new heavy rail connecting the airport to the CBD, close to the multi-media complex and sporting facilities at Moore Park, and ocean beaches beyond, the area is ripe for redevelopment. Indeed, significant residential development occurred in the area throughout the 1990s, drawing on underutilized and semi-derelict industrial sites. The development in question envisaged almost 12,000 new dwellings, catering for a range of income groups. The relevant Local Environment
Plan (LEP) and development control plan imposed responsibilities on potential developers with respect to the minimum provision of affordable housing, similar to City West. The contribution could be in the form of actual dwellings or their monetary equivalent, and was set at 3 per cent of residential floor space and 1 per cent of non-residential space for each developer application.

In 1999 a large developer (Meriton Apartments Pty Limited) appealed the inclusionary zoning provisions of the LEP. The subsequent judgment found in favour of the developer, casting doubt on the viability of inclusionary zoning as a means of achieving affordability outcomes in N.S.W. However, the judgment also invalidated the entire LEP, effectively returning the planning status of Green Square to industrial land use. The developer appealed this decision and the state government appealed the original decision. In an attempt to resolve the uncertainty now created around inclusionary zoning for purposes like affordable housing, the government twice amended the Environmental Planning and Assessment Act (most recently in June 2000) to enshrine this intent. It is likely that this will enable local Councils to impose affordability provisions on future residential and mixed-use developments, and avoid the specific grounds for objection allowed in the Meriton Green Square case.

What the Green Square case does highlight is the very narrow interpretation placed by state planning jurisdictions on ‘developer contributions’. In general, such levies must be closely tied to basic underlying physical and social infrastructure facilities. This, as noted below, is not the case in some other countries.

The Queensland Housing Department has also embarked on a wide-ranging review of planning and other approaches to increasing the supply of affordable housing. The Department recently released a detailed strategy paper on the subject, with a January 2001 response date. Both local government and regional planning systems are being targeted as potential mechanisms for encouraging the provision of affordable housing. Voluntary statutory covenants can already be attached to land for this purpose, under the Land Titles Act, 1993. The Department has formed a joint Inner City Affordable Housing Taskforce with the Brisbane City council (BCC) resulting in an agreed statement of key planning policy matters and a (current) examination of the feasibility of a joint Affordable housing Trust (Departmental communication).

E. Ethical Investment

Ethical investors are individuals or organizations who invest in order to secure a mix of commercial and non-commercial (social) returns. Their defining characteristic is that they willingly and knowingly accept less than the going commercial (risk adjusted) rate of return on their investments in order to also achieve the social returns they value. (Ethical investments are, therefore, to be distinguished from ‘economically targeted investments’ [ETIs] that deliver appropriate risk adjusted rates of return in addition to collateral economic and social benefits [Jobling, 1994]).

Community housing organizations have always depended on this form of investment, often through donations of the land component by churches and charitable organizations and individuals. Such an approach is, inevitably, small scale and ad-hoc, dependent on where the land is located. Recently, Ecumenical Housing Inc. has developed a ‘partial debt finance model’ (PDF) to formalize the approach. In this model private finance at market rates is required for that part of the land-house package not donated. The rents required to meet the interest and operating costs can therefore be lower than in a fully commercial situation – how much lower depending on the loan to value ratio and the interest rate level.

In line with general developments in the financial sector, in Australia and internationally, ethical investment is growing as a distinct phenomenon. Ecumenical Housing Inc. has developed an Equity Investment/Headleasing model (EIH) to target this growing market. Dwellings are constructed and sold to social investors at cost, who lease them back to community housing
organizations at an agreed rent below market levels. Rental yield is generally 3 per cent or less, compared to average market rental yields around 6 to 7 per cent. Investors receive most of their return in the form of capital gains. Both the PDF and EIH models depend for maximum effect, on low income tenants having access to substantial Commonwealth benefits, including rent assistance, and/or investors willing to accept substantially lower than market rates of return. (Both models are detailed in McNelis, 1999).

Some of the larger, established community housing organizations are also actively exploring links with ethical investors, both individual and institutional. In Victoria, Supported Housing Development Foundation (incorporating Singleton Pty Limited) has been operating a shared equity model for more than ten years in order to house people with one or multiple disabilities. Disabled residents or their families contribute part of the equity (or, alternatively, a no-interest loan) to finance the dwelling managed by the Foundation. The disabled resident gains by securing long term (life-time) tenure of the dwelling at a rent set to cover the cost of financing the other share and ordinary property and administrative expenses. Currently, the Foundation is exploring the potential to access emerging institutional sources of both ethical funds (e.g. Bendigo Bank) and economically targeted investments (e.g. the Transport Accident Commission of Victoria which is charged with meeting the long term housing needs of brain damaged road victims).

Porter (2000) also gives the example of Perth-based community housing organization, City Housing, which is seeking to provide affordable housing financed by zero-coupon debentures. In other words, investors would receive capital gains only on the properties acquired using these funds. Families and support agencies providing for people with disabilities are, as in Victoria, targets for such a model.

Ethical investing has developed faster and further in a number of other countries, than in Australia. In the United States, what has been termed ‘socially responsible investing’ (SRI) exceeded US$2 trillion in 1999 – almost one in every eight dollars invested in equities. Dow Jones has teamed with the asset management company, SAM Sustainability Group, to produce a suite of regionally and industry specific indexes that report on the financial performance of included companies (see www.sustainability-index.com).

Mutual and pension funds are also screened to certify that their investment practices meet specified criteria. Negative screens establish that investments are not being made in socially or environmentally dubious industries, like tobacco products, gambling, and weapons. Positive screens privilege investments in benign environmental and social areas like energy efficiency, sustainable land management, and housing.

The appearance of SRI is a much more recent and modest development in Australian financial markets, compared to both the US and Europe. Including church investments, the current volume of SRIs here has been estimated at about $1 billion (Allen Consulting Group, 2000). The limited impact to date stems from a number of factors, including lack of scale in local markets, the dominant role of the (environmentally invasive) mining and resources sector (in the Australian economy and equity market) and persistent beliefs among Australian investors that SRIs necessarily deliver relatively low returns. In fact, on this last point, research shows that screened funds often outperform unscreened funds on conventional financial benchmarks. For example, in the US a pool of ethically screened funds out-performed conventional funds by over 30 per cent over the past 1, 3, 5 and 10 year periods (quoted in Saleeba, 2000, p. 13). Closer to home, Australian Ethical Investments has delivered annual returns of more than 20 per cent over the past three years, double that of the All Ords Accumulation Index (ibid.). A possible underlying reason for these differences is that well managed, socially responsible companies are perceived to lower the risk of expensive future liabilities with respect to environmental or human health impacts, and that markets are rewarding those companies with lower cost of finance (Allen Consulting Group, 2000).
The large industry superannuation fund, HESTA, recently launched an environmentally screened investment fund, Eco-Pool, supported by Westpac Investment Management (WIM). WIM has also developed a screened fund – Eco-Share – with Monash University’s Centre for Environmental Management. By the end of the current year it is estimated that Eco-Share will have about $100 million under management. These organisations also produce Australia’s first environmental financial index, the Eco-Index, covering our better eco-rated companies.

As knowledge of the impressive relative economic performance of SRI-type investment percolates through financial markets, investor interest is likely to increase. Interest will be further fanned by widespread attitudes in the community in favour of SRI and by both greater investor choice and shareholder activism around corporate governance issues. A recent study by Resnik-KPMG found that 69% of Australians surveyed indicated support for their superannuation funds investing in SRIs (quoted in the ethical investor newsletter, 21 August 2000; see www.ethicalinvestor.com.au).

The implication to be drawn for affordable housing is that, to the extent that positively screened investment funds explicitly include housing as a preferred option, a potentially rapidly growing source of private funding is at hand. On the general SRI front, Allen Consulting Group’s (2000) summary report, Socially Responsible Investment in Australia, concludes: ‘Socially Responsible Investment in Australia is on the verge of a transition from being a niche market to having a place in the mainstream.’

4.4 International Experience

Private, and especially institutional investment in affordable housing has developed much faster and further in a number of other OECD countries encouraged by government policy. Selective examples are presented below to indicate the range and scale of these alternative developments, and to demonstrate how other jurisdictions have sought to overcome the barriers to greater private sector investment in affordable housing.

4.4.1 United States

The U.S. has a long tradition of government supported financial assistance for affordable rental and home purchase, utilizing sophisticated market techniques, in a context where conventional public housing represents only about 1 per cent of the total housing stock. These policy approaches involve all levels of government and have included: a raft of taxation subsidies (negative gearing, high building allowances, income tax credits); housing bonds; land and housing trusts; community banks and development corporations; secondary mortgage markets; housing vouchers; subsidized loan interest rates; shared equity/option to buy schemes.

The dominant housing finance institution in the U.S. is the Federal National Mortgage Associated (Fannie Mae), established in the 1930s and (together with two other like organizations, Ginnie Mae and Freddie Mae) responsible for the explosive growth of secondary mortgage markets. Fannie Mae now facilitates the organization of about one-seventh of all mortgage loans in the U.S. through the issue of mortgage backed securities (MBSs), biased towards assisting lower income households into home ownership.

There are also many community-based non-profit organizations operating at the local and regional level committed to assisting people with low to moderate incomes into owner occupation. Box 2 describes one example. In general, such organizations seek to bring representatives together from local (or State) government, the private sector and the non-profit sector to leverage expertise, contacts and access to funding sources. These partnerships generally provide more than finance, for example, financial counseling and education programs,
technical assistance on design and construction, etc. Other non-profit organizations like community development corporations operate home purchase deposit assistance programs, matching an individual’s savings in designated accounts with top-up grants, reminiscent of the Australian Government’s home savings grant schemes (for details see, Stegman, 1999, ch. 2).

Affordable rental housing has also been targeted by a range of government initiatives at all levels, but particularly dependent on Federal government subsidies of one form or another.

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<td><strong>Wilmington Housing Partnership Corporation (Wilmington, Delaware)</strong></td>
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The WHP is a joint venture organization managed by a mayor-appointed Board comprising city officials and representatives of the private and non-profit sectors. It was established in 1989 to assist in raising the home ownership rate in the city towards 60 per cent, while encouraging high quality housing design, the rehabilitation of existing properties and greater local participation in civic affairs by disadvantaged businesses and non-profit organizations. Total funding of about US$8 million has been raised from ethical investors, charitable foundations and government. Since 1994 WHP has provided home purchase deposit and transaction cost assistance to 300 households and supported the development of 200 new and 250 renovated dwellings. (Source: Stegman, 1999, pp. 7-10).

Between 1965 and 1983 nearly 1.5 million dwellings were developed for rental to subsidized tenants at controlled (low) rents. Assistance to investors came in the form of rent subsidies (vouchers), low interest loans, mortgage insurance and tax benefits delivered by accelerated depreciation. These ‘section 8’ dwellings, as they became known, were locked into the low rent market segment for a minimum of twenty years, thereafter investors were free to withdraw their dwellings from the scheme. The scheme was closed to further expansion during the early years of the Reagan Presidency. Since then, the number of rental dwellings involved has gradually fallen as individual investors opted out. Stegman (1999, p. 127) estimates that by the year 2006 a further 700,000 dwellings will be potentially lost as the rental subsidy contracts expire. The Federal Department of Housing and Urban Development is seeking to renegotiate extensions of these arrangements to keep the dwellings concerned from filtering out of the affordable market segment – though using this opportunity to both reduce what are now seen as overly generous subsidy levels and enforce improved housing standards.

Of central importance to the supply of affordable housing in the U.S. has been the operation of the Community Reinvestment Act (CRA), enacted in 1977. The CRA requires all Federally regulated banking financial institutions to meet the full range of community credit needs. In practice this means the requirement to invest in the provision of a range of basic infrastructural needs to sections of the population ‘underserviced’ by banks and other mainstream institutions. Access to affordable housing by low income households and other minority groups is included within the scope of the CRA. Since its introduction, US$400 billion has been directed towards traditionally underserviced populations, more than 80 per cent provided since 1992, in response to the much tougher government regulations on public disclosure by financial institutions imposed since that date (Freedman, 1998)\(^\text{14}\)

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\(^\text{14}\) The full disclosure rules were demanded of the banks and other financial institutions by the Congress in return for the US$300 billion taxpayer bail-out of the failed savings and loans (‘thrifts’) sector following their deregulation in the 1980s and subsequent mass failures.
CRA-inspired mortgage loans for affordable owner occupation share one or more of the following features characteristic of all affordable loan products (by comparison to conventional loans) in the U.S. (Stegman, 1999, pp. 184-5):

- reduced down payment (deposit)
- higher loan-to-value rates
- flexible employment (income) history hurdle
- reduced cash reserves
- reduced interest rates
- private mortgage insurance exemption
- reduced transaction costs.

These features increase access to owner occupation across a broader spectrum of the population allowing the lender to claim CRA status, important (given the Federal Government’s regulatory imprimatur) in enhancing its credit worthiness. Quercia (1977) has found that banks offering affordable loan products in low income neighbourhoods as part of their overall activities perform as well, on average, as banks which do not.

CRA-driven investment also flows into affordable rental housing, facilitated by taxation subsidies delivered to real estate investment trusts. REITs are trusts that distribute virtually all their earnings to their shareholders, along with capital gains on dwelling sales. Both these income flows are taxed at the shareholder’s individual rate, but the REIT pays no tax on its earnings. Rents can therefore be lower than the market level while still returning normal income flows to shareholders. Investment by ethical investors can reduce rents further. (See Box 3) This situation contrasts markedly with the taxation regime facing residential rental trusts in Australia, post 1987 (see section 4.3, above).

### Box 3

**The Community Development Trust, Inc.**

CDT was established in 1998 as a self-managed REIT to provide a range of debt and equity products that meet CRA requirements, and will finance owner occupation, multi-unit rental dwellings, community facilities and commercial properties in low income areas. The trust operates nationally in order to build up a spatially diversified property portfolio. The investors include a number of banks, insurance companies and a newly formed organization, the Local Initiative Support Corporation (LISC). Debt investments will be focused both on affordable housing and local community development projects, with equity concentrated in the acquisition of federally subsidized dwellings (old section 8 stock in risk of filtering out of the affordable sector). LISC has acquired all the Class A shares for US$1.5 million. Class B shares have been offered to a limited number of institutional investors and banks with a minimum subscription of $100,000. CDT aims to:

- provide shareholders with a commercial rate of return;
- foster affordable housing and community development;
- provide a diversity of investment outlet by investing in different cities, communities and neighbourhoods, and in non-metropolitan regions;
- stimulate further housing and community development in areas invested in, strengthening the local economic and community base.

(Source: Stegman, 1999, pp. 192-3).
Important as the CRA has been for affordable housing, other policy initiatives have emerged. With the phasing out of the old section 8 subsidy program, ‘(t)he Low-Income Housing Tax Credit (LIHTC) program, which is now over ten years old, has become the nation’s primary mechanism for encouraging production of housing to be occupied by low – or moderate – income households’ (McClure, 2000, p. 91).

The LIHTC program was introduced in the Tax Reform Act of 1986, in part to allay concerns about the declining stock of affordable housing as a result of capping the section 8 program. Since then up to 900,000 dwellings have been constructed or redeveloped under this program (Cummins and DiPasquale, 1999), at around 70,000 per year. The program delivers tax credits to selected developers who must contract to maintain low to moderate income occupancy of the dwellings for a period of 30 years. Key features of the program are:

- developments do not qualify for tax credits unless either at least 20 per cent of units are occupied by tenants with a household income less than 50 per cent of the metropolitan median household income or at least 40 per cent of units are occupied by households receiving less than 60 per cent of the metropolitan median household income;
- rents charged (plus utility expenses) must not exceed 30 per cent of metropolitan-wide household income and expense benchmarks. This limits rent levels but does not ensure that all tenants will pay 30 per cent or less of their household incomes;
- investors have the option of converting dwellings after 15 years to the general rental market, but must sell the property to another investor willing to maintain it in the rent/income restricted market if such an investor offers an appropriate price (based on a statutory formula) within a year of notice to convert. The sitting tenant must also be given the option to remain at the restricted rent for 3 years after notice to convert. In effect, the minimum period that a dwelling must be maintained in the LIHTC program is 18 years not 30 years;
- tax credits are federally financed subsidies delivered through state government housing finance agencies. Each state has an annual quota of credits to distribute, equal to US$1.25 per capita (of state population). This means that, in total, some US$350-370 million of annual credits can be allocated nationally;
- potential developer-investors compete to secure the state allocations. Each state prepares a ‘qualified allocation plan’ setting out the criteria and procedure for allocating credits;
- a number of states supplement federally provided credits by offering ‘top up’ credits on state income tax, offering further scope to reduce rents on projects receiving both sources of subsidy;
- several key recent federal taxation rulings have strengthened the incentive structure of the LIHTC program. For example, in 1997 it was determined that section 8 rent assistance (housing vouchers) and public housing operating subsidies could be packaged in (re)developments without losing LIHTC subsidies. A further ruling allowed banks to invest in pooled housing equity funds (as well as direct property) receiving tax credits while still retaining their CRA credit status.

Recent evaluations of the performance and effectiveness of the LIHTC program have concluded:

- average rents on tax credit dwellings are 9 per cent lower than the national rental average (Stegman, 1999, p. 72). Both are substantially higher than rent levels in other subsidized programs, especially public housing;
- the average income of tenants assisted under the program was 37 per cent of the area median, well below the statutory median but above the income levels of those in most hardship (U.S. General Accounting Office, 1997);
- on average, 46 per cent of the development cost of the projects was covered by equity raised through the allocation of tax credits, 38 per cent by first mortgage loans and the remaining 16 per cent by a collection of other subsidies (Cummins and DiPasquale, 1999). This suggests that, given the rents that can be charged under the LIHTC program, the tax credits are insufficient by themselves to stimulate development;
• the subsidiary program goal of ‘social mix’ has not been achieved. Most LIHTC developments are uniformly low income in nature, with tax credits applied to all units. This reflects the fact that two-thirds or more of qualifying developments are located in poor neighbourhoods (McClure, 2000, pp. 97-8);
• some 60 per cent of projects have involved new construction and 40 per cent redevelopment or rehabilitation. This reflects the greater credit rate pertaining to new construction (ibid., p. 98).

In summary, the Low Income Housing Tax Credit Program appears to have a mixed scorecard. Early in its history critics charged that some of the credits were being siphoned off in the form of extra investor returns, rather than being fully applied to lowering rents (Stegman, 1991). Greater competition among potential developers seeking the credits, and tighter administration seems to have largely resolved this problem (McClure, 2000, pp. 106-108; Stegman, [1999, p. 73] now accepts this conclusion). Rent levels are somewhat lower than market benchmarks but not dramatically so and dwellings produced under the program are not reaching those in greatest hardship. McClure (2000, p. 100) summarises the program’s impact as follows:

The tax credit program appears to have been absorbed into the rental housing development process, but it has not been adopted by market-rate housing developers. Rather, it has been adopted by either non-profit CDCs [community development corporations] or by specialized developers building projects entirely dedicated to low – or moderate – income occupancy. The units are going into largely metropolitan markets containing large concentrations of poor, minority households but rents are being charged that make the units affordable to only those poor households with the highest incomes in these areas. [But see Box 4 for two state government attempts to broaden the clientele and goals sought under the program].

<table>
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<th>Box 4</th>
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**Targeting housing to the elderly and people with special needs**

The State of Kansas has developed a QAP that emphasized the provision of dwellings in rural areas for elderly tenants and others with special needs. Proposals received priority ‘bonus points’ in the allocation of available credits if they meet all the building requirements of both the Americans with Disabilities Act and the American National Standards Institute. Developers must also provide and maintain a range of on-site accessibility devices for residents with disabilities in 10 per cent of units in order to gain priority allocation. Further points are awarded to developments to be located near retail, medical and community facilities.

**Targeting mixed-income housing projects**

The State of Indiana has reserved 25 per cent of its tax credits for developments in the 25 largest cities. Points are awarded to developments in which at least 2 per cent of tenants receive incomes less than 40 per cent of area median income. Points are also awarded if up to 50 per cent of units are reserved for tenants paying full market rents. Bonus points are awarded if both targets are met, providing a strong incentive for developers to provide for a diverse income mix.

(Source: Stegman, 1999, p. 86).
A number of U.S. cities also use town planning controls to increase (or offset the loss of) affordable housing in their jurisdictions. Inclusionary zoning and linkage fees are among the mechanisms used. For example, in return for development consent, the City and County of San Francisco requires the inclusion of affordable housing units in all developments of more than 10 dwellings. The proportion of units to be set aside as affordable depends on the private benefit delivered to the developer through density bonuses, reduction of car parking spaces, etc. The affordable dwellings can be built on-site, elsewhere or an in lieu contribution made in cash. The dwellings are targeted to home owners and tenants with incomes up to 60 per cent of the area median. (Further detailed examples are provided in Lawson, 1995).

4.4.2 United Kingdom

Historically, affordable housing in Britain has been directly provided by the state, financed by central government and managed by local councils. By 1980 council housing represented about one-third of the total stock. Private renting had shrunk to less than 10 per cent. Over the last 20 years major housing policy changes have wrought significant change in the nature of the British housing system. The council housing sector has shrunk, while home ownership has increased, along with community housing (housing associations) and – more modestly – private renting.

The Housing Act of 1980, enacted by the first Thatcher government introduced the right-to-buy for public tenants. By the mid-1990s 1.5 million public housing dwellings had been sold to tenants at subsidised values. The 1988 Housing Act introduced mechanisms for ‘de-municipalising’ social housing by allowing the stock to be transferred to housing association management. By 1995, 185,000 former council dwellings had been transferred to housing associations (Kleinman, 1996, p. 37). At the current moment the Cities of Glasgow and Birmingham are considering whether to transfer their entire stock, totalling around 200,000 dwellings, to the large housing associations.

Thus, the dual thrust of policy has been to move those households who could afford it into home ownership, supported by continuing, albeit sharply declining tax subsidies and income protection mortgage insurance, while shifting more of the burden of social housing provision to a growing housing association sector. The private rental sector was earmarked for modest growth with modest supply-side subsidies and more generous rent assistance in the form of the housing benefit for low income tenants. Housing benefit is also available to housing association residents, while the associations receive capital grants which have fallen from 100 per cent of new dwelling development costs to about 50 to 60 per cent, over the past decade.

Housing associations raise the remainder of finance for new dwellings from institutional sources, both through a special purpose government intermediary – the Housing Finance Corporation – and by direct borrowing from the banks (MacLennan and More, 1996). Hence, institutional involvement is almost entirely through debt not equity investment (Whitehead et al., 1994; Whitehead, 1997). This lending flow into what is, in reality, an arm of government (given the implicit guarantees inherent in the sector) only avoids inclusion in normal public borrowing limits by a British Treasury dispensation, something that has not been forthcoming in Australia.

In 1988 the Business Expansion Scheme was extended to cover investment in residential rental companies. Investors received tax relief on funds subscribed up to a maximum amount. The shares in the company had to be held for at least five years. Thereafter, dwellings could be sold and capital gains realised free of tax. The schemes were phased out in the 1990s and made little impact (Kleinman, 1996; Crook and Kemp, 1991).

A second scheme involving the creation of housing investment trusts (HITs) was introduced in 1996 by the Major Government. HITs are tax-favoured equity vehicles, listed on the stock
exchange, designed to attract investors seeking indirect rather than direct investment in residential property. Tax subsidies are delivered by charging company income tax at the small company rate (24 per cent) and exempting them from capital gains tax.

Crook and Kemp (1999) recently carried out a survey of 27 financial institutions and property companies, 18 of whom they had interviewed in 1994 before the introduction of HITs. The aim of both surveys had been to determine investor attitudes to investing in private rental housing.

The 1999 survey found that HITs had made little impact. They were considered to be unduly constrained by program restrictions concerning capital value limits, not fully tax transparent, offering insufficient liquidity (in spite of listing) and inadequate returns. In other words, this innovation had apparently not adequately surmounted the barriers to institutional investment discussed in section 3.6, below. However, by comparison to 1994, the later survey did uncover significantly more interest in residential property among these investors, and some activity. Major findings included:

- Institutions differed in their preferences for direct versus indirect ownership. Those institutions already investing had opted for direct ownership but those considering entering this field preferred indirect vehicles. For the latter, the main considerations were liquidity, scale, tax transparency and good quality housing management. The main limitation perceived here was the absence of large residential property companies. This meant that investors required a ‘novelty’ premium on the rate of return, compared to the established commercial property market.
- Two of the six insurance companies interviewed had invested directly in rental housing and two more were considering indirect vehicles, as were two of the four pension (superannuation) funds interviewed.
- The potential equity investors stressed the income earning and portfolio diversification benefits of residential lettings. Rents were seen to rise in line with prices and earnings over the long run. Moreover, diversification benefits were believed to flow from the partial disjuncture of commercial and residential property cycles.
- A number of the institutions interviewed suggested that investing in the middle or upper ends of the residential market was less risky than at the bottom or low rent end.
- The banks and building societies interviewed were only interested in debt financing rental housing. There seemed to be few limitations on the potential future growth of debt financing in this sector, apart from considerations of the credit risk of borrowers.
- The main remaining barriers to equity investment in rental housing are: market risks (revenue and residual value); the small scale nature of the industry; high transaction costs; difficulties in assembling a large, diversified portfolio to produce an adequate overall return; poor quality management, and; inadequate market information. Political risk was seen to be less of a problem at the end of the decade, suggesting that investors believe that both major political parties are committed to encouraging the future development of a private rental sector.

The report concludes that significant institutional equity investment in this sector will not occur, except in niche markets, until these barriers are further reduced and residential property companies grow to a scale of operation, diversification and professional management that deliver adequate returns. To facilitate this process, the report recommends two policy changes. First, create transparent 'Tax Exempt Residential Lettings Schemes' or TERLS, in which untaxed net earnings flow directly to investors to be taxed at their individual rates (similar to REITs in the United States). Second, introduce and enforce industry-wide codes of practice setting out minimum standards for the management and maintenance of rental dwellings. This would give investors confidence that their assets would be protected and their reputations not sullied by association with ‘slum housing’.
4.4.3 The Netherlands

By the early 1990s 42 per cent of the Dutch housing stock was located in the social housing sector, three quarters of that managed by some 1100 housing associations. A further 13 per cent of the stock is privately rented. Housing associations are non-profits that are expected to play a leading role in the construction and management of affordable housing in the Netherlands. They have, historically, received significant subsidies for construction and operation of the stock and via rental allowances to social housing tenants. In 1988 construction subsidies on new dwellings were removed and in the 1990s operating subsidies have been phased out (or, more accurately, converted) as part of a ‘grossing and balancing’ exercise whereby future operating subsidies were capitalized and applied to discharging housing association loans on the existing stock. In effect, the central government has made a one-off equity grant to the sector which is now responsible for managing and expanding the stock to meet housing needs.

Insurance companies and pension funds have long lent to the sector. Under the new arrangements, the banks are now keen lenders drawn by the strong and diverse equity base of the housing associations and a complex, tripartite system of insurance and government guarantees. First, associations must maintain an equity base at a minimum benchmark of the book value of their housing assets. Second, loans to individual associations are guaranteed by the WSW, a fund set up for the purpose by an initial government grant and on-going contributions from member associations. It was estimated that by 2000 guaranteed assets would reach 100 billion guilders ($72 billion) (Boulhouwer, 1997, p. 18). A second organization, the CFV Mutual Fund, has also been established by member contributions to aid individual associations which fall into financial difficulties. Third, ultimate responsibility for housing delivery rests with local and central government which are expected to share some of the cost with CFV in restructuring and rescuing housing associations experiencing otherwise terminal financial difficulties. In consequence, the strong and deep pattern of self-insurance and final guarantee has reduced the cost of borrowed funds substantially, leaving it about 25 basis points above the ruling government bond rate (ibid.). In the late 1990s new social housing was 85 to 90 per cent funded by loans from the institutions. Because of the ‘grossing and balancing’ policy there has been little scope or need for private equity investment in the sector. However, criticisms levied at the new arrangements include concern for the upward creep in housing association rents, by comparison to both past levels and public housing rents.

The private rental sector has declined since 1970 and stood at 13 per cent of the stock in 1995, about the same size as the public housing sector managed by local government. Institutional investors own about 350,000 dwellings (6 per cent of total stock), almost as many as individual investors. The institutions concerned are largely the pension funds and insurance companies seeking to match cash flows with their long term liabilities. Interestingly, the institutions have been less active than individual investors in selling their stock to local authorities, housing associations and owner occupiers over the past 20 years (Oxley and Smith, 1996, p. 150).

4.4.4 Other Western European Countries

The situation throughout Western Europe is complex and differentiated. In general, however, most countries have moderate to large social housing sectors and significant private rental sectors, both of which draw some mix of government subsidies, including tax relief, construction and operating subsidies. In Germany, for example, it is difficult to distinguish private and socially rented stock. Over a million socially rented dwellings are in fact, privately owned. Private landlords receive a number of tax advantages, including negative gearing and accelerated depreciation – viz. since 1989, the building allowance of newly constructed rental dwellings is 7 per cent per annum for the first four years, 5 per cent for the next four years, phasing down to 2 per cent after 17 years (Oxley and Smith, 1996, p. 14). This means that 58 per cent of the cost
of a new dwelling can be claimed as an income tax deduction in the first 10 years after construction – compared to 25 per cent in Australia.

Housing standards and tenant rights are also, in general, protected in most Western European countries, somewhat offsetting the attractiveness of rental housing to private investors. This is especially so in countries like Germany, where a form of rent control (actually, constraints on how quickly and how much rents can be raised) was introduced in the 1970s, and which the tax subsidy reforms of 1989 were designed to ameliorate.

The detailed nature of the similarities and differences in the provision of affordable housing across Europe are canvassed in the references listed in Box 5.

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<th>Box 5</th>
<th>Key references on European approaches</th>
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4.5. Key Australian Studies

The findings of a number of relevant Australian studies carried out over the past 10 years are selectively summarized in this section.


This paper argued that the preceding 15 years had witnessed a slow decline in the private rental sector in the capital cities, particularly at the low cost end of the market. The paper identifies the small-scale nature of rental investment and the withdrawal of corporate investment in favour of commercial property and other assets. Most of these conclusions have been supported by the subsequent research and ABS rental investor surveys carried out later in the 1990s and noted in section 3.2, above. The pattern of investment in this sector was, the paper argues, closely associated with the existing taxation regimes – particularly, land tax thresholds, capital gains tax impacts and the low building allowance level. Consequently, policy changes recommended focused on taxation changes. In particular, ‘(t)he use of targeted depreciation allowances, particularly through syndicated forms of investment, appears to represent the most effective means of increasing the supply of low to moderately priced private rental housing’ (Brian Elton & Associates, 1991, p. XV). The paper went on to claim that a ‘key feature of syndicated forms of investments is the potential for attracting new sources of capital to private rental investment such as superannuation funds and life insurance companies’ (ibid.).

The paper proposes several criteria that measures to stimulate greater investment in affordable rental housing should meet – namely, they should:

- shift investment into housing stock likely to be occupied by low-to-moderate income households;
help to bridge the current yield gap between rental housing and other investments (including other property assets);
stimulate investment in new dwellings rather than (or in addition to) existing dwellings;
target stock type, as well as investor type;
complement planning policies which are aimed at increasing diversity of the housing stock and housing choices;
be efficient – i.e. cost effective for government;
produce no adverse (perverse) effects elsewhere in the housing system.


The Caversham report reviewed the likely level of private investment needed to adequately fund a social housing sector, and the limits to raising those funds. The dollar figures they came up with are dated but a number of their conclusions are still relevant. In particular, the report argued that investors, particularly the institutions, are interested in real rate financing. A major barrier here was that the (then existing) indexation treatment of capital gains for taxation was not easily transferred from individual investors to pooled equity or corporate structures. The report concluded:

A real rate funding is a relatively new sector of the market and appeals only to a limited but growing number of investors in certain sectors, there is a finite amount available – particularly under existing taxation and market conditions... The potential for raising further funds via current structures is very uncertain... Sufficient funds could not be raised utilizing currently available techniques and instruments, to finance the anticipated net private funding requirement of SHAs at current subsidy levels (quoted in Hall et al., 1995, p. 7).

The report goes on to recommend that a single issuer of real rate (indexed) debt securities should be established to raise funds for social housing for all the States and Territories. The taxation situation should be clarified so that the indexation benefits of the then CGT could be passed on to investors, thereby lowering borrowing rates. Finally, funds raised in this manner for social housing should be declared to be outside the Loan Council limits and therefore not impinge on scarce public borrowing capacity.


This study presents and evaluates three financial models for the provision of subsidized housing that could be targeted towards young households:

- a debt model – financed by Commonwealth borrowing, the dwellings to be managed by the Commonwealth. Both fixed and variable rate loans, indexed and standard, were analyzed (including CPI Indexed and housing price indexed variants);
- a leasing model – dwellings owned by the private sector and headleased to the Commonwealth;
- a corporate vehicle – which purchases dwellings and leases to youth housing organizations. The vehicle attracts both equity and debt investment from the private sector, and the Commonwealth provides subordinated debt to enhance credit risk (of the former).
In each case, the assumptions concerning interest rate levels, transaction costs, rates and the taxation situation of the participating individual and institutional investors are specified. The models were run over the medium (10 years) and longer term (25 years) and the net cost per tenancy to the Commonwealth and State governments calculated in net present value terms (i.e. after tax payable to or foregone by government has been accounted for).

The main conclusions of the modeling were:

- the total subsidy cost per dwelling before tax is allowed for is lowest for the fixed and floating rate options of the debt model, where the whole subsidy cost is borne by the Commonwealth. Headleasing, by comparison, is very costly, exceeded only by the housing price indexed debt option. The company structure model performs ‘in the middle’, better than headleasing, worse than the non-indexed debt options;
- the total subsidy cost after tax savings swings in favour of the company structure model utilizing fixed or variable rate debt. This structure drawing on CPI indexed debt is also marginally cheaper than the fixed and variable rate options of the debt model. HPI debt funding blows out the subsidy cost for the Commonwealth in the case of the debt model and the States for the company structure or corporate vehicle model. Again, headleasing falls in the middle;
- considering the net subsidy cost per tenant per year, the cost to the Commonwealth ranges from $235 (company with floating rate) to $2,588 (company with HPI debt). For the States the range is $222 (any of the company options) to $2,912 (HPI debt structure). The variable rate company option delivers a total annual subsidy cost to both levels of government under $500, less than $10 per week. These subsidy levels are quite moderate, especially when compared to, say, rent assistance levels and trends.

The study also modeled ‘best case’ and ‘worst case’ scenarios, with respect to key parameters like interest and inflation rates, construction price trends and rent inflation. Key results were:

- The riskiest option for the Commonwealth is the variable rate debt model which offers both the best and worst (i.e. most volatile) outcomes. This is also a relatively risky option for the States, though for them the headleasing model delivers the highest cost in the worst case;
- in the worst case headleasing minimizes the Commonwealth’s subsidy cost, but the company structure with variable rate debt minimizes State costs. If a superannuation investor holds variable rate debt, however, this option would be the most risk averse strategy for the Commonwealth;
- the net subsidy outcomes per tenant per year (given the parameter values tested) range from a ‘profit’ of $2,599 to a cost of $1,515 for the Commonwealth and from a profit of $2,040 to a cost of $2,682 for the states. In other words, the upside risk can deliver negative subsidies or revenue for government;
- combining the after tax outcomes of the Commonwealth and States, the least risky option is the company structure with floating rate debt, producing a worst case cost of $2,075 per tenant per year, 58 per cent of the worst case for the floating rate debt model. In the former (company) case the Commonwealth bears most of the risk.

4.5.4 *East Perth Redevelopment Authority, Affordable Housing Proposal, EPRA, Perth, 1995*

In 1995 an affordable housing shared equity model was developed for the East Perth Redevelopment Authority (EPRA) for submission under the Commonwealth’s (then) social housing subsidy scheme. The scheme, which was phased out soon after, provided Commonwealth subsidies over a period of time to support joint private-public sector projects.
The EPRA proposal drew on and would have run parallel to Homeswest’s established shared equity program, which had a substantial waiting list.

The proposal was framed in the context of constructing 50 medium density dwellings distributed through the East Perth redevelopment Area in inner-Perth.

This model structure had five critical components,

- A private investor/investors to provide finance for the construction component, in return for an equity interest of 68%.
- Homeswest Keystart loans to tenants for the purchase of 20% equity.
- A residual equity of 12% by the EPRA.
- A Manager and Agent for the private investor and EPRA.
- Establishment of an EPRA Sinking Fund to provide rental subsidies, over which the investor has a charge to ensure the guaranteed rental yield.

Tenants with household incomes in the $28,000-$33,000 range would be targeted.

The details of the structure are outlined, below, in box 6.

Under this structure investors would be invited to purchase a share of the dwellings at a deemed (land plus construction) price and lease back the dwellings to tenants in exchange for the EPRA guaranteeing a rental yield. To ensure this rental yield the Investor would be given a charge over the sinking fund to the extent that the fund would pay any shortfall between the guaranteed rental yield and the net rents received. At the end of the ten years the tenants loans would be fully paid out and the tenant would be given the first option to purchase the remaining equity at market price determined by valuation. Failing the exercise of this option by the tenant the tenant will be required to consent to the sale of the dwelling and the distribution of equity shares to the various parties. The price to be paid for the guaranteed rental yield would be tendered in the market.

The Investor and the EPRA would pay a Manager a fee equivalent to 5% of the gross rents and the Investor would be responsible for all rates and, maintenance expenses up to a value of 1% of the Investor’s equity share (after which maintenance costs would be to the account of the tenant).

The tenants would each obtain a loan from Keystart for a 20% equity share, leaving 12% equity to EPRA.

The Manager and Agent would determine initial tenant eligibility, remit the mortgage capital to EPRA, receive all payments, carry out maintenance and collect both rent and mortgage payments as one payment. To assist credit recovery a default of any part of the combined payment would constitute a default of the whole. The Manager and agent would be responsible for remitting mortgage payments to Keystart and rents to Investors, calculating shortfall subsidy amounts and maintaining mortgage management.

This paper summarises the issues raised by private sector investment in affordable housing and reviews relevant recent and on-going research. Debt and equity options are explored and a number of examples, most of which are noted in section 3.3, above, briefly described. The study points to the absence of institutional investors (other than through the secondary mortgage market), which it attributes to inadequate income yields, illiquidity and poor credit quality.

The major issue highlighted is for community housing organizations to increase net rental yields, both by maximizing rental income through a mixed income resident base and more efficient management practices. Even so, to ensure rents are affordable, government subsidies will need to be factored in, raising issues of transparency and accountability.

Tentative recommendations – ‘the preferred approach’ – are that:

- debt finance options may be better than equity models in the immediate term since they face lower existing barriers and sector capacity constraints and provide community housing organizations (CHOs) with more control over the stock;
- fixed rate borrowing is less risky for CHOws than floating or variable rates. If property structured, inflation indexed (real rate) loans can produce a close match between cash income and outgoings;
• there was significant CHO support for a sector-wide borrowing vehicle to acquire dwellings that are managed by individual CHOs (the South Australian solution) and for mortgage finance to individual organizations;
• models that mix government grants and private finance are probably necessary given that private sector-only models tend to depend on optimistic assumptions about capital gains and/or tax benefits;
• a major effort must be put into establishing the infrastructure for a viable CHO sector. This will entail significant development of organizational capacity and financial knowledge throughout the sector. Effective risk management structures will need to be implemented to reassure potential private investors that financial targets will be met.

4.5.6 Ecumenical Housing Inc., Private Funding Models for Church Community Housing, National Churches Community Housing Network, Melbourne, 1999.

This study – the National Churches Community Housing Project – was carried out by Ecumenical Housing Inc. It focused on the scope for small scale investment in affordable housing by the Churches or other ethical or social investors.

Two models were developed (both noted in section 3.3, above): a partial debt finance model (PDF) and an equity investment/headleasing model (EIH). The PDF model assumed a benchmark return to investors equal to the post-tax nominal rate of interest on long term bank deposits. The second model depends on equity finance and the benchmark assumed was the post-tax real rate of interest on long term bank deposits.

Both models are targeted towards tenants eligible for rent assistance and assume rents to be 25 per cent of income (include RA), provided the required rent does not exceed current market levels. First mortgage claim to the dwelling provides the private investor with a high degree of security. The major risk borne by the church which provides the land or equivalent is mortgage default due to poor housing management; this risk can be managed by appointing a highly competent community housing organization to manage the scheme. The major risks borne by the latter are inadequate rental income and future changes in government housing subsidy policy; the first risk can be managed by instituting efficient tenant selection and rent collection processes, the latter by securing bipartisan government commitments to a transparent and consistent policy framework.

The EIH model entails an established and competent community housing organization negotiating a sale and leaseback arrangement with an ethical investor, the term of the lease negotiable up to 15 years. The equity investor receives a return made up of capital gains, tax benefits and small rental yield. As holder of equity the ethical investor bears a range of risks (e.g. inflation, changing tax treatment, capital gain levels, etc.). The risks borne by the housing manager are similar to the PDF model. The model is very sensitive to the capital gain assumed. The higher the capital gain, the lower the required rent and the more affordable the housing for lower income households.

The main results of the PDF modeling were:

• across the three scenarios (broadly reflecting the ratio of land value to construction cost in Sydney, Melbourne and Adelaide, respectively) the model requires the loan-to-value ratio to be less than 65 per cent. At higher LTVs, required rent exceeds market rent. In low value land areas (the Adelaide case) donation of land by a church group may be inadequate to fund a viable project; an extra cash injection may be required;
• assuming a real annual capital gain of 1 per cent and a 60 per cent LTV, required rent was 8-11 per cent below market rent, depending on the size of the dwelling. If LTV fell to 55 per
cent, the rent discount rose to between 11 and 18 per cent. With zero real capital gain and a 60 per cent LTV, required rent just exceeded market rent.

The main results of the EIH modeling were:

- in all scenarios the equity investor receives a rate of return at least as high as the benchmark long term real bank deposit rate when rental yield is 1 per cent (assuming zero real capital gain);
- this base case situation is slightly worse for the investor who negatively gears the dwelling; however, all scenarios meet the benchmark return or better at a rental yield of 2 per cent (and 1 per cent real capital gain);
- however, the results are highly sensitive to the underlying parameters in the case of negatively geared investors, and much more stable for the full equity investor;
- with a 3 per cent rental yield, (base case) required rents are from 18 to 24 per cent below market levels, extending affordability significantly down the income scale.

4.5.7 M. Berry, J. Flood, J. Fisher and M. Lindfield, Development of Investment Models Aimed at Encouraging Institutional Investment in Rental Housing, report to the Department of Family and Community Services, Australian Housing and Urban Research Institute, Melbourne, 1999.

Selective interviews with insurance companies, banks, superannuation funds and funds managers have been carried out in a number of studies (Coopers and Lybrand, 1996; Hall et al., 1995; Berry et al., 1999) focused on their attitudes to investing in rental housing and affordable rental housing in particular. The basic conclusion of such studies is that many institutional investors are interested in diversifying their portfolios into this property class but only if suitable debt and equity instruments are available and subject to reduction of a number of barriers. Some of the issues raised include:

- there is a growing shortage of domestic fixed interest securities due to constraints on public borrowing. The superannuation funds, in particular, are looking for alternatives to government debt at a suitable premium on the government bond rate. There was interest in inflation-indexed bonds but suspicion of securities indexed to housing prices because of doubts as to the quality of property value data;
- investors are prepared to enter joint ventures but must be confident in the financial viability, expertise and commitment of partners;
- specific barriers to greater investment in affordable housing perceived by the institutional investors were: high management costs entailed, the problem of achieving a viable scale of project and investment, inadequate rental yields, bad publicity, illiquidity, poor market information and political risk. Many of these perceived barriers reflected similar views found in Crook and Kemp’s (1999) British study;
- location of investment is critical to investment vehicles dependent on capital gains, both with respect to the selection of individual sites and the construction of an appropriate portfolio diversified by location, dwelling type and quality;
- there is some receptivity to debt leveraged corporate equity vehicles, preferably listed.

In relation to this last point, Berry et al. (1999) model net (after tax) returns to equity investors in a hypothetical (new) medium density rental development in a middle suburb of Brisbane in the mid-1990s. A 10 per cent after-tax return on equity was assumed, based on industry estimates. Inflation was assumed to be low (2 per cent) and rents to rise in line with inflation over the 20 year investment period. In the base case dwellings were financed by a 30:70 per cent equity/fixed interest debt split. Real capital gain was set at 1 per cent.

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In this case the required rent necessary to meet investor target rates of return was in the order of 20 to 25 per cent above ruling market rents, a clear indication of the scale of the rent yield gap dissuading institutional investors from entering this market.

The yield gap – in relation to equity investors – could be reduced or eliminated in the model by one or a combination of the following factors:

- achieving a higher capital gain (at least 2 per cent real, other parameters unchanged);
- higher inflation (the risk borne by fixed interest investors);
- reduced cost of loan finance by drawing on a combination of capital indexed and annuity indexed bonds which better match cash flows generated by the scheme;
- government subsidies delivered to the equity investor.

If required rent is brought down below market rent by such means, specific mechanisms would need to be implemented to ensure that these gains are passed on to tenants in the form of actual rents. Otherwise, rents would be set at full market levels and equity investors pocket the extra gain.


This report updates the 1998 report summarized in section 3.5.5, above, looking at initiatives and relevant developments over the past two years. As the decade of the 1990s ended the investment climate in Australia was characterized by relatively low inflation, short term investment horizons and progressive tax reform regarding indirect taxation and capital gains tax, with further changes in business taxation signposted. The study restates a number of requirements that must be met if significant private investment is to flow to community housing organizations, including:

- creation of adequate income streams or rental yields in excess of operating costs;
- appropriate management and risk management strategies to ensure firm financial control and protection against default;
- support/leverage through adequate commitment of government funds;
- mechanisms in place to parcel up private funds in large, cost effective trenches.

The study briefly surveys several umbrella and one-off approaches, including some noted above. One recent example quoted refers to a joint venture between Community Housing Canberra and a large private developer which entails the redevelopment and sale of a run-down public housing complex to produce a mix of private and social housing. This suggests that a viable market niche for community housing organizations may be offered by joint ventures designed to regenerate rapidly obsolescing and increasingly difficult to let public housing estates.

A second recent initiative described is Perth’s City Housing which has borrowed to fund land purchase, assisted by capital construction subsidies from Western Australia’s SHA, Homewest. The problem of mortgage lenders requiring a guarantee from government or the directors of the community housing organization has been side-stepped by an agreement with state government to buy the dwellings should City Housing default on the loan.

The study stresses the strategic importance for the community housing sector of ‘scaling up’, and of government supporting a limited number of larger or umbrella organizations. Further emphasis on raising management and service standards across the sector is vital, in line with the new national community housing standards framework and move towards a nationally consistent system of accreditation of providers. Ecumenical Housing Inc. is setting up a new company with
involvement by major banks and investment banks to demonstrate best practice in and broker affordable housing schemes drawing on private finance.

A clear conclusion of the research briefly noted by this study is that government’s role is central in encouraging a greater flow of private investment into social housing and that even existing levels of subsidy could leverage an increased volume of affordable housing if government’s various roles and contributions can be clarified and strategically developed.

4.5.9 Landcom, Report on Centreacre Public Benevolent Institution (PBI) model for Affordable Housing, Sydney, 2000.

In 1999, Centreacre – a church based welfare organization – approached N.S.W. Landcom with a proposed model for affordable housing. The model is based on a joint venture between private investors and tax-exempt public benevolent institutions. Landcom has commissioned a detailed analysis of the feasibility of this approach. At this stage, only a summary of Landcom’s review is available. Details of the model structure have not yet been made available to the authors of this report. However, it appears that the model depends on the private investor contributing part of the initial investment in the form of a ‘donation’ that is immediately deductible against other taxable income with the remainder committed to generate an investment income flow over an agreed period. The dividend or interest returns are, in turn, donated back the PBI and tax deductible in the year of receipt. Investor return is, presumably, comprised of a mix of tax benefits and capital gains.

Initial legal advice suggests that a favourable product ruling may be achieved from the Australian Taxation Office, failing that, specific legislative change to the Taxation Assessment Act would be required. In the latter case a number of possible changes can be envisaged, each producing a stream of tax benefits that could underwrite lower-than-market rents; e.g. a greater-than-100 per cent deduction for investment contributions, or a specific amendment allowing full deductibility in the year in which the contribution is made.

The Landcom review stresses the importance of gaining strong political support for the approach from the Commonwealth Department of Family and Community Services and the Treasury. Critical here is the need to demonstrate that significant direct and indirect returns – e.g. in lower future rent assistance and other social security payments – will flow from the introduction of the model, and that there will be no net loss of taxation revenue.

Financial modeling on the sensitivity of key parameters was found to meet the risk-return profiles of potential investors. The potential scale of this new market is difficult to gauge. However, other tax effective products in the agricultural land area currently draw about $1 billion of investment funds annually. As a maximum ballpark estimate the review suggests a flow of $5 billion annually into PBI-type developments would produce over 22,000 dwellings, about half of which could be let at affordable rents. This latter outcome would come close to matching annual increases in the public housing stock before the sharp decline in growth in that sector over the past few years.
4.6 A Summary of Current Barriers to Institutional Investment in Affordable Rental Housing

Based on the studies reported in preceding sections, it is possible to identify the major barriers currently hampering or preventing a significant flow of investment funds into the rental market.
(i) **Low returns**
It was noted above that gross rental yields currently average between 5 and 7 per cent and a high proportion of individual investors reap negative or zero net returns. Unless very significant capital gains and tax savings are anticipated, rental investment in the current market environment will not return the after tax return on equity (in particular) that institutional investors currently require for this class of investment. In essence, the ‘cottage industry’ nature of the rental housing industry, with its diverse range of investor types and motivations, is not attractive to large institutional investors who have different and more sophisticated perceptions of risk, a wider range of investment opportunities and much more intense pressures to maximise risk adjusted returns over their whole portfolios, than do small individual landlords.

(ii) **High Risks**
Of course, low returns would not be such a problem if the risks were also low. However, there are significant risks pertaining to rental investment in housing, including revenue risks associated with uncertain vacancy rates and maintenance costs. Volatility of net returns also arises from uncertainty over future capital gains, the perceived prevalence of poor property and tenant management practices and the possible impacts of future changes in government policy, including future taxation treatments of depreciation, capital gains and property values.

(iii) **High Management Costs**
The small-scale nature of the industry currently generates limited opportunities for economies of scale and scope in management. The commitment of large ‘tranches’ of investment by the institutions, ideal means of rationalising and reducing management costs per dwelling, raises new financial intermediation costs and design risk associated with the creation of new financial instruments and organisational structures. The institutional investor is interested in the level and certainty of calculable cash flows, not in the actual management of rental dwellings. Thus, an appropriately structured ‘vehicle’ or structure must stand between the institutions and the tenants, managing the latter and delivering tax-efficient returns to the former.

(iv) **Illiquidity**
All property investments are illiquid compared to equities and bonds. Nevertheless, the institutions have a large and diverse time-dated volume of liabilities, and a capacity to invest for varying lengths of time in a well diversified portfolio. Illiquidity is not, therefore, a decisive stumbling block, as is demonstrated by the well established asset class of commercial property attracting anything up to 20 per cent of an institution’s funds. If anything, residential property is less illiquid than commercial property, since there is a deeper secondary market and the unit size of the asset is generally smaller. However, investors will require some premium on the rate of return to compensate for the relative difficulty and cost involved in ‘take out’.

(v) **Poor market information**
Although there is a deep secondary market for dwellings, it is highly segmented - by quality, location, neighbourhood environment, size and type - and unevenly monitored. The existing series available on dwelling price movements are incomplete, often unreliable and not available over the long period, compared to the century or more of high quality market information on equities, for example. It is therefore more difficult for investors and investment managers to accurately price risk in the case of residential property. This is a major deterrent to investment, especially by superannuation funds which must meet stringent, legally enforced standards in the allocation of their funds across asset classes.

(vi) **No Track record**
Structured deals like PEP1 and PEP2 are few and far between. Innovations proposed, like equity bonds or securitised rental leases, have no established track records in Australia. There will be a premium required on the rate of return for any new financial asset until it demonstrates
its return and risk characteristics in the market place - or, alternatively, government guarantees may be required in the initial phase of launching new financial assets.

These factors, taken together, ensure that the rental stream required to meet the risk-adjusted rate of return required by institutional investors is significantly higher than ruling market rents. This required rent reflects all the current risks perceived by investors relative to risks and returns available across a range of investment opportunities. The primary aim, then, of any policy designed to encourage institutional involvement in this sector is to close that rent yield gap. Both the rent gap and possible means of closing it are represented in Figure 3.

The difference between required and market rent has been termed ‘the market rent gap’. This will differ for different market segments and over time, reflecting both conditions in local property markets and general conditions in the economy. However, market rent will – as has been documented in earlier sections of this report – often exceed affordable levels for some households. In that case it is the difference between required rent and affordable rent – here termed ‘the affordable rent gap’ – that is significant for policy. If institutional investors are to be attracted, in volume, into rental housing then the market rent gap must be closed. However, if the resulting housing is to be affordable then the remainder of the affordable rent gap must also be removed.

Figure 3 suggests one of the two main ways of closing the gaps – viz. bridging the difference with a mix of government subsidies, for example, Commonwealth rent assistance and state government relief of stamp duty or land tax. In the figure presented, subsidies are shown as more than closing out the market rent gap – therefore making it financially viable for institutions to invest in housing. However, the combined subsidy is not sufficient, in this depiction, to reduce required rent to affordable levels. Tenants would be required to pay in excess of an affordable rent, say, 35% of income, rather than the conventional 30% benchmark. To fully remove the affordable rent gap governments would need to commit sufficient subsidies in one form or another.

The second way of closing the gap is to reduce the required rent by reducing risks facing investors; this could be managed, for example, by provision of government guarantees or improvement in property market information and intelligence capacities.

Figure 3: The Affordability Rent Gap

![Diagram of the Affordability Rent Gap](image-url)
These possible strategies for ‘closing the gap’ are summarised in Box 7, and explained below. They are not mutually exclusive and combinations of strategies could be adopted to engineer lower rents.

1. **Government Subsidies**

The most visible and direct form of subsidy is a cash payment, in this case to tenants under the rent assistance program of the Commonwealth. Other cash subsidies could be envisaged, both from state government and as income flows paid directly to investors or the vehicles providing affordable housing. This latter practice occurs in Britain with respect to some housing associations. Key issues concern eligibility and the dangers (to government’s fiscal position) of a ‘blow-out’ in payments.

Tax subsidies, such as those offered in the US through the Low Income Housing Tax Credit Scheme, depend on the legislative will of the responsible government. The key issues are targeting and indirect effects on investment patterns through the economy and implications for government revenue.

Town planning approaches like inclusionary zoning and linkage fees are most likely to be implemented at state and local government levels in federal systems such as Australia. They tend to be tailored to local conditions and political realities.
Box 7 Strategies for closing the gaps

(1) government subsidies
   - cash
   - tax
   - planning
   - land

(2) efficiencies
   - operational
   - financing

(3) risk reduction through
   - govt. guarantees
   - insurance
   - improved market
   - data on performance

(4) enhanced residual value of the asset (capital gain)

(5) government prescription
   - prescribed assets
   - ratio (or threat)
   - tax surcharge
Governments are large urban land owners and land will often comprise 40% or more of the total investment in housing. Much of this land bank will be located in high value and growth areas. Governments can apply their land to affordable housing either in the form of equity to the project or at a subsidised (less than market value) rate. In the latter case, issues to do with public accountability involving Auditors General and Valuers General may need to be dealt with.

2. Greater Efficiencies
Housing management systems may be designed to maximise cost savings in constructing and managing dwelling portfolios for the investment vehicle. This would involve the application to the housing sector of systems and approaches like computer aided design, automated purchasing and scheduling, just-in-time inventory control, e-marketing, electronic asset management programs and so on. The scope for applying and reaping savings from such approaches is unclear but could be determined. Other factors impinging on operational efficiency in the sector relate to continued attempts, especially by state governments, to streamline and improve land development and construction regulatory systems relating to residential subdivision, building control and certification.

The other main source of potential cost savings concerns financing housing developments. Reductions in cost of finance can be passed on in lower rents. By better matching cash flows to investor liabilities finance cost can be shaved. This may involve the use of a mix of debt and “dequity” instruments, including indexed products of various types. The increasingly sophisticated capital market is a forcing-house for innovative financial products.

3. Risk Reduction Strategies
The most straight-forward means of reducing risk to investors is by allocating it to government in the form of a guarantee. As the earlier discussion noted, such measures have been used in a number of the states in the past in order to get joint ventures off the ground with private investors. The form of the guarantee, who gives it and under what terms will determine the efficacy of the measure in reducing private risk and, therefore, required rent. In Australia, under current policy settings, it will also have implications for governments’ public borrowing limits and the taxation position of investors.

Risk can also be efficiently allocated through insurance arrangements. For a fee certain risks like rental default can be transferred to another party better able to bear them. If risk is efficiently priced by financial markets there will be a net savings that can be passed onto tenants in lower rents.

In the absence of good quality, complete and consistent data on the market performance of housing as an asset type, rational investors demand an ‘uncertainty premium’ for investing in housing as opposed, say, to local or international equities. This premium could be reduced or eliminated if investors could fully trust property market data over the longer term.

4. Enhanced Residual Value
The main offset for rental yield is capital gain on disposal of the dwellings. Where good market information is available investors will be able to make accurate predictions of future property values and structure their investments accordingly. By diversifying investment across dwelling types and locations, with an investment horizon that is long enough to encompass two or more property cycles, even in a small market like Australia, substantial capital gains on property portfolios can be factored in at relatively low risk. This also assumes that effective asset management practices are in place to protect residual value through adequate maintenance, etc.
5. **Government Prescription**
Prior to the deregulation of the financial system in Australia governments imposed a range of direct controls over the asset structure of financial institutions. For example, minimum proportions of the assets held by life insurance companies had to be in liquid and government securities. Similarly, the savings banks, as they were, could only invest in home loans and government securities. Paralleling trends elsewhere in the Western world, Australia progressively removed these and related controls through the 1980s. However, government as the sovereign authority is at liberty to reimpose direct controls – i.e. to prescribe specific asset ratios that must be met by designated investment organisations like the superannuation funds. In this context it would mean a legislative requirement to invest a minimum proportion of superannuation fund savings in affordable housing. What qualifies as ‘affordable housing’ for purposes of the regulations would, of course, have to be fully specified. Superannuation trustees would require the force of legislative change to enable them to invest in this manner while still meeting their onerous fiduciary and other duties as trustees of other people’s welfare.
References


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The estimate of required capital is based on the weighted average actual construction or spot purchase costs for public housing dwellings in all States in 1998/99. The table below sets out the relevant data.

**Average Costs of Construction Of Public Housing Stock 1998-1999: $000’s**

<table>
<thead>
<tr>
<th>State</th>
<th>Construction Cost</th>
<th>Spot Purchase</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>New South Wales</td>
<td>79</td>
<td>125</td>
<td>102</td>
</tr>
<tr>
<td>Victoria</td>
<td>109</td>
<td>125</td>
<td>117</td>
</tr>
<tr>
<td>Queensland</td>
<td>91</td>
<td>171</td>
<td>131</td>
</tr>
<tr>
<td>Western Australia</td>
<td>100</td>
<td>133</td>
<td>116.5</td>
</tr>
<tr>
<td>South Australia</td>
<td>104</td>
<td>103</td>
<td>103.5</td>
</tr>
<tr>
<td>Tasmania</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
</tr>
<tr>
<td>Northern Territory</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
</tr>
<tr>
<td>All States</td>
<td>97.60</td>
<td>141.87</td>
<td>119.73</td>
</tr>
</tbody>
</table>