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Submission to the December 2020 Review of the operation of the National Housing Finance and Investment Corporation Act 2018

AUSTRALIAN HOUSING AND URBAN RESEARCH INSTITUTE

Contents

About AHURI

As the only organisation in Australia dedicated exclusively to housing, homelessness, cities and related urban research, AHURI is a unique venture. Through our national network of university research partners, we undertake research leading to the advancement of knowledge on key policy and practice issues.

AHURI research informs the decision-making of all levels of government, non-government sectors (both private and not-for-profit), peak organisations and the community, and stimulates debate in the media and the broader Australian community.

Our mission is to inform and impact better housing, homelessness, cities and related urban outcomes through the delivery and dissemination of relevant and authoritative research. To achieve this mission we deliver four key programs.

National Housing Research Program

AHURI's National Housing Research Program (NHRP) invests around $4 million each year in high quality policy-oriented housing research and associated activities. We broker engagement between policy makers, key stakeholders and researchers. This allows us to undertake research that is immediately relevant and actively contributes to national housing policy development.

Our network of university research partners conducts research on key policy issues utilising a variety of research activities. This ensures the flexibility to undertake longer-term projects when fundamental research is needed, while also responding quickly to new strategic policy issues as they arise.

Australian Cities Research Program

AHURI is actively broadening its scope to consider the role, functioning and policy questions facing Australian cities. We are enhancing our significant evidence base on housing and homelessness policy and solutions, and consolidating our role in delivering integrated and robust evidence to guide policy development. We are investing in and developing partnerships for an Australian Cities Research Program. AHURI is working with governments and relevant stakeholders to expand our role in delivering research that informs urban policy and the shaping of cities in Australia.

Professional Services

AHURI Professional Services draws on our in-depth understanding of housing, homelessness, cities and urban policy and the expertise of AHURI's national network of Research Centres. We deliver evidence reviews and synthesis, policy engagement and transfer, and are experts in research management and brokerage.

Conferences, events and engagement

Our conferences, events and communications stimulate professional and public dialogue. We disseminate research in innovative ways and engage with government, private, not-for-profit sectors and the community.

National Network of AHURI Research Centres

There are currently nine AHURI Research Centres across Australia:

- AHURI Research Centre—Curtin University
- AHURI Research Centre—Monash University
- AHURI Research Centre—RMIT University
- AHURI Research Centre—Swinburne University of Technology
- AHURI Research Centre—The University of Adelaide
- AHURI Research Centre—The University of South Australia
- AHURI Research Centre—The University of New South Wales
- AHURI Research Centre—The University of Sydney
- AHURI Research Centre—University of Tasmania.

The impact of the National Housing Finance and Investment Corporation (NHFIC) on the Community Housing Provider (CHP) Sector

The Community Housing sector has been growing in scale and profile for a number of years (Milligan et al, 2017). Growth in community housing provision has been based on transfer of stock from (State owned) public housing and on development of new stock by community housing providers. Increasingly, this new stock is developed through partnerships involving commercial developers, state governments, or both.

NHFIC has the potential to improve housing outcomes through social bonds, to the extent that Community Housing Providers (CHPs) are constrained in undertaking new construction, or new construction at scale, due to lack of finance. AHURI research has found that CHPs raise commercial debt to finance construction, fund turn-key acquisition, or refinance existing loans (Muir, et al, 2017). The AHURI research found that construction finance is much higher in risk for the lender due to non-completion hazards. This research identified that: 'some community housing organisations' debt facilities covered a construction period for two years, converting to an operating loan upon project completion' (Muir et al, 2017: 31).

However, participants in an AHURI Investigative Panel reported that construction finance is in general difficult to secure in Australia (Milligan et al, 2013), and this has driven many CHPs toward purchasing turn-key developments from the open market rather than constructing their own purpose-built housing (Lawson et al, 2014a). The construction of new housing stock by public and community housing providers continues to be modest in Australia.

Provision of government grants and guarantees are important to facilitating finance, particularly for smaller CHPs that have more difficulty attaining financing that large CHPs. AHURI research has shown that CHPs who had raised construction-period finance found that significant government funding of development costs had unlocked banks' willingness to lend. Banks derive comfort from the understanding that the government will intervene to stave off or respond to a borrower default, even if this pledge is explicitly limited to nominating another CHP to step in (Lawson et al 2014a). A key role of intermediaries such as the NHFIC should be to assess the risks and benefits of applications for borrowing money from individual CHPs. For the system to have credibility and accountability, CHPs and regulators need to have: 'high calibre and professional expertise in financial management'. Management also requires 'adherence to clear and appropriate commercial benchmarks for solvency ratios, interest rate cover and equity to be eligible for any guarantee' (Lawson et al 2014a: 17).

To date AHBA loans have been awarded to large scale CHPs, providing them with more favourable financing than they might otherwise attain. However, these organisations would have been able to gain financing in the absence of AHBA. To maximise the benefit of AHBA loans in generating new supply, NHFIC might consider targeting AHBA loans to some of the smaller CHPs that are less able to negotiate favourable loan conditions from commercial lenders.

The Role of NHFIC in Housing Supply

The Australian Government's current position is that provision of social and affordable housing is a State and Territory responsibility. The Australian Government provides indirect support for provision of community housing through a government guarantee on NHFIC's social bonds, which provide a mechanism for private sector finance of social housing development.

Critical to NHFIC's operation is to mitigate any risk associated with investment along with offering a government guarantee to investors to reduce their risk exposure. AHURI research has identified a list of principles for NHFIC to adhere to (boundaries in permitting eligible projects, lowering risk, transparency and commitment, expert intermediary, scale and frequency of bond issues and adequate structure) to address risks. For example, in relation to an adequate structure, the guarantee scheme should have clear and agreed structure including targets, volume caps, contestable allocation, on-going compliance process and 'trigger points', practical lines of defence against default, mechanisms to build up contingency reserves and agreed loss sharing arrangements (Lawson et al 2014a).

Providing a government guarantee is part of reducing perceived risks for investors. AHURI research found that for adequate rate of return, 'in mid-2011, Housing Supply Bonds (HSBs) would have had to yield around 8–9 per cent to attract self-managed retirement funds. Any lower yield would have to be offset by either a tax concession advantage (substantial enough to lift yields to an adequate level of return) or by a high rating, reflecting a low risk. This is why enhancements (e.g. government guarantees or tax incentives) are required to reduce risk and improve HSB yields' (Lawson et al 2014a).

Evidence from AHURI research, in reviewing international guarantee schemes, suggests that a government guarantee would reduce the borrowing rate and reduce uncertainty for investors. The research found that 'it overcomes many of the barriers to investment in affordable housing by offering investment opportunities at an appropriate scale, simplicity and risk weighted return. It is also attractive to housing providers because of its lower cost. The government guarantee would help establish a robust and competitive investment market' (Lawson et al 2014b).

The AHURI research concludes that guarantees have had a minimal impact on government budgets, with most boasting a zero default record and a few even provide a return for government. The UK's The Housing Finance Corporation (THFC) has reportedly 'harnessed the lowest cost long-term private investment for registered social landlords in the history of private investment in social housing. With the government guarantee, they offered 28 years of credit at 3.76 per cent interest cost, being only 0.37 per cent over the long-term government bond rate. The THFC issue was three times over-subscribed by investors' (Lawson et al 2014b). The first round of NHFIC's social bonds were oversubscribed at a similar rate, supporting the applicability of this research.

EY analysis suggests 'CHPs could achieve pricing benefits of up to 1.4 per cent p.a. based on a like for like comparison with the bank market' (EY Canberra 2017: 12). Similarly, AHURI research found that in the Netherlands, the Dutch Guarantee Fund Social Housing has reduced interest rates by 1–1.5 per cent below the going equivalent mortgage rate (Lawson et al, 2014a).

The guarantee scheme was proposed in a 2014 AHURI report, assuming the intermediary would raise $7 billion to finance 20,000 dwellings (Lawson et al 2014c). On the basis of what retail and institutional investors required, the bonds were allocated 70 per cent to AAA bonds, 20 per cent to Tax Smart bonds and 10 per cent to NAHA growth bonds. As a result, the average cost of funds available for on-lending to CHPs was 4.7 per cent, considerably lower than the then current costs of around 8.2 per cent (usually required by self-funded retirees). An additional allowance would need to be made for costs incurred by the financial intermediary in raising and distributing these funds (Lawson et al 2014c).

AHURI research has concluded that a condition of any guarantee is that the Government would need to give a clear commitment to continuity of funding eligible tenants, for example via CRA, and the term of the guarantee, so that potential investors can be confident of a pipeline of future bond issues. NHFIC could negotiate and sign an overarching agreement with government(s) offering an issue-specific default guarantee on bonds issued by the Agency. The clear commitment to policies and programs ensures a stable operating environment, such as adequate supply incentives and revenue side subsidies (Lawson 2014a).

In short, long term policy continuity in maintaining the government guarantee is crucial to the continuing success of the Affordable Housing Bond Aggregator.

The Role of NHFIC in Increasing Homeownership

The First Home Loan Deposit Scheme is designed to provide a limited number (initially 10,000) loan guarantees per year to eligible first home buyers. There are a number of relevant research findings in AHURI's published evidence base that are pertinent to the design and intent of this scheme.

AHURI research (Parkinson et al. 2019) shows that aspirations for home ownership remain high among young people but many feel it is out of their grasp:

- 70 per cent of early adults aspire to owner-occupation and nearly two-thirds (61%) of those with a tertiary educated member in their household believed it to be possible to purchase within five years.
- however many with lower education don't believe these aspirations are realisable over that period—around 42 per cent of those with an education to year 11 or below thought that home ownership was impossible, they had no intention or they were unsure.

AHURI research (James et al. 2019) shows that the lack of a deposit is an issue for older Australians

- 61 per cent of older Australians aged 55–64 cited lack of a deposit as a barrier to long term housing aspirations, the most important barrier of all cited. This was also an issue for those aged 65–74 and those 75 years and above.

There have been many programs to support first home owners but the evidence provides limited support for their effectiveness.

The broad idea of improving deposit assistance for first home purchasers is not new. AHURI research (Hulse et al. 2010) has shown that initiatives have included:

Relaxation of minimum deposit requirements among some lenders

- Introduction of First Home Owner Grants (FHOG) since 2000—providing a lump sum to help purchasers buy their first owner occupied property
- State/territory assistance such as exemptions on stamp duty, loan guarantee schemes, and shared equity programs such as Keystart in Western Australia and Homestart in South Australia.
- Deposit saving schemes such as First Home Owner Accounts (designated accounts for households saving for a deposit which attract a partial co-payment from the government as well as tax advantages) and the First Home Super Saving Scheme which enables people to build a deposit inside their superannuation fund through voluntary contributions.

There are few publicly available evaluations of the effectiveness of first home buyer schemes. Rigorous evaluation of the First Home Loan Deposit Scheme would provide a useful contribution to knowledge on effectiveness of such programs.

One previous AHURI study showed that government programs like FHOG can be successful in enabling first home purchasers to enter home ownership earlier (Wood et al. 2003). They have been successful partly because they have eased the deposit constraints of first home purchasers, especially when the grants were set at a more generous level than they are at present.

Beyond that study there have otherwise been few publicly available evaluations of the other schemes, including those involving housing deposit guarantees or saving schemes. Research has not demonstrated that these schemes increase homeownership—rather, they allow some first home buyers to enter homeownership earlier than otherwise might have occurred.

AHURI research has documented organisations, such as Keystart, responsible for innovative home ownership programs and home loan guarantees, although mainly in the context of shared equity products (Pinnegar et al. 2009). This research demonstrates that:

- Programs should be well targeted
- Schemes directed to help first home purchasers should be appropriately targeted so as to facilitate sufficient take-up of the scheme without providing assistance to those who do not need it, or who would be better off receiving alternate assistance.
- The high maximum income limits provided in the NHFIC scheme appear generous, and would include most persons able to afford home ownership. It is not clear how these limits were set and whether the scheme will be otherwise prioritised to those on lower incomes or on a first come first served basis. The inclusion of house price caps are intended to provide some brake on the scheme pushing up house prices.
- Modelling by AHURI of the FHOG found that provision of the grant enables many home buyers to purchase in the short run, but many of those purchasers would have been able to purchase at a later date (Wood et al. 2003). The subsidies do not substantially assist lower income households who might not have otherwise been able to access the home ownership market (other mechanisms, like shared equity schemes are recommended for this purpose).
- A valid question remains about the value of home ownership for those on low incomes. Low to moderate income purchasers have been increasingly constrained to purchase in outer urban areas. Although they have built wealth, house prices in these areas have not increased as quickly as houses in middle and inner urban areas (Hulse et al. 2010). On the other hand, an increasing number of young people appear unable to access home ownership and will be unable to access its wealth building opportunities (Yates, 2008; Flood and Baker, 2010).

NHFIC's 2019-20 Annual Report indicated that 6,814 scheme participants had signed a contract by June 2020. This figure represents around 5% of the annual number of first home buyers. It is not possible to state how many of these participants would not have achieved home ownership in the absence of the scheme, or how much earlier these households reached ownership than they would otherwise have done.

The Role of NHFIC Research

The National Housing Finance and Investment Corporation Amendment Bill 2019 amended the *National Housing Finance and Investment Corporation Act 2018* to “enable the NHFIC to undertake research into housing affordability in Australia, including housing supply and demand”[1].

NHFIC programs should be supported by high quality research and relevant evidence. It is important that the various programs NHFIC operate are supported by high quality research. AHURI recognises the importance of a comprehensive, contemporary evidence base and up to date data on housing supply, demand and affordability.

To this end, AHURI’s acquittal report for the 2017-2018 funding period proposed to Treasury the development of an Australian Housing Markets Council. The proposal was that this council would operate in a manner similar to the National Housing Supply Council (abolished in 2013), but with a broader remit—to consider not only housing supply, but also housing demands (underlying, expressed and projected) and a nuanced consideration of stock type and quality in Australia’s macro and micro housing markets.

While this proposal was intended as a program of AHURI, it very closely resembles the NHFIC research function identified in the amendment bill. AHURI strongly supports the creation of this research function and has actively supported with NHFIC in its delivery.

It is notable that the December 2020 Review terms of reference refer only to “undertaking research into housing affordability”, and do not refer to housing supply or demand. AHURI note that these terms are not interchangeable – that housing supply, housing demand and housing affordability are distinct topics, with different underlying drivers. The fundamental gap in Australian housing data (and therefore research) relates to housing supply and demand, rather than affordability.

AHURI has provided support to NHFIC in developing the research function. This has included ongoing advice, as well as completing research for NHFIC to develop measures of the social impact of NHFIC’s bond loans to social housing providers (a requirement of the International Capital Market Association’s Social Bond Principles), so that the true benefits of the investment are understood.

Primary research is unlikely to be a substantive role for NHFIC, primary research can be more efficiently conducted and funded elsewhere (by AHURI, the Proiductivity Commission, and through the Australian Research Council).

A more meaningful and less duplicative contribution could be made by instead focusing on dataset development. This could complement the existing housing datasets held by the Australian Bureau of Statistics (ABS), the Australian Institute of Health and Welfare (AIHW) the Australian Urban Research Infrastructure Network (AURIN) and the emerging Australian Housing System Data Platform.

1 National Housing Finance and Investment Corporation Amendment Bill 2019. https://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bId=r6402

NHFIC is uniquely placed to provide data generated by its programs, and to coordinate their evaluation. This could include:

- Modelling of risks to lenders of default under the First Home Loan Deposit Scheme
- Evaluation of intervention on housing outcomes for low and middle income households of guarantee schemes
- Evaluating impacts of the schemes on consumers and wider stakeholders.

NHFIC's programs — the Affordable Housing Bond Aggregator, the National Housing Infrastructure Facility, and the First Home Loan Deposit Scheme — generate unique data that could be leveraged by researchers with relevant expertise to generate new knowledge on housing outcomes for Australians supported by these programs. AHURI is able to facilitate access to these researchers through our national research network of nine universities.

AHURI can further assist the NHFIC in these activities, as well as in establishing research or dataset development priorities.

The Governance and Operation of NHFIC

AHURI research supports that a governing expert Board of Directors requires directors with extensive experience and expertise in financial management and credit assessment along with community housing provider representation (Lawson et al, 2014a). The current NHFIC Board of Directors covers these areas of expertise; AHURI is be pleased to offer assistance in identifying potential future Directors.

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