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Incentivising small-scale investors to supply affordable private rental housing

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Acronyms and abbreviations used in this report

ABS	Australian Bureau of Statistics
AHURI	Australian Housing and Urban Research Institute Limited
APRA	Australian Prudential Regulatory Authority
ATO	Australian Tax Office
CGT	Capital gains tax
CHP	Community housing provider
CIM	Conscious Investment Management
CRA	Commonwealth Rent Assistance
DCE	Discrete choice experiment
LTHI	Long-term hold investor
NAHA	National Affordable Housing Agreement
NRAS	National Rental Affordability Scheme
PRA	Private rental assistance
PRAP	Private Rental Assistance Program
PRBP	Private rental brokerage programs
PRS	Private rental sector
RTA	Residential Tenancies Act
SEREA	Social Enterprise Real Estate Agencies
SHP	Social housing provider
SP	Stated preference (experiment)
SRA	Social rental agencies
STHCGI	Short-term hold for capital gain investor
STL	Short-term let

Glossary

A list of definitions for terms commonly used by AHURI is available on the AHURI website ahuri.edu.au/glossary.

Executive summary

Key points

- **Small-scale investors can be incentivised to enter the affordable housing market through financial incentives that prioritise positive cashflow.**
- **Make-good provisions that ensure property is returned to the landlord in original condition will increase participation in affordable private rental schemes.**
- **Communication and education programs will increase successful long-term participation.**
- **Headleasing is an effective way to attract small-scale investors and increase affordable rental housing stock.**
- **Small-scale investment-support schemes should prioritise long-term hold investors over 'flippers' and short-term lets.**
- **Community housing providers are preferred over private investors, however they are unable to provide the quantity and diversity of housing stock required to meet demand.**

Key findings

The Australian housing market is experiencing both long-term structural changes and short-term pandemic impacts. The result is rising rents and very low vacancy rates as demand for rental housing outstrips supply—particularly for low-income households (Reynolds, Parkinson et al. 2024). The private rental sector has become the fastest-growing part of the Australian housing system, outstripping household growth since 2001 (Hulse, Reynolds et al. 2019).

This research seeks to understand how governments might incentivise small-scale investors to provide affordable rental housing. We used a mixed-methods approach, incorporating a quantitative survey of 800 small-scale investors, in-depth interviews with small-scale investors, and focus groups with policy makers to identify potential policy options. The survey sample is broadly representative of small-scale investors in Australia, however our sample tends to be younger and have higher incomes than the average Australian small-scale investor. The qualitative engagement we conducted comprised relatively small sample sizes; it was used to refine and contextualise the survey results.

Positive cashflow

As a group, small-scale investors own the majority of residential rental dwellings in Australia, but generally own only one to two investment properties each. These investors are highly sensitive to short-term cashflow; approximately 46 per cent of survey respondents ranked positive cashflow as their most important investment strategy. Long-term hold investors (LTHI) are impacted by unexpected extrinsic financial factors—such as rising interest rates and tenant vacancies—and could not afford to be negatively geared when they experienced financial hardship. Rental guarantees are also important to this group; they are 12 per cent more likely to participate in a scheme that offers guaranteed rental income. Similarly, our qualitative engagement found that this group values indexing rents to market rates. Incentives that prioritise cashflow will motivate this large group of investors.

Make-good provisions

Aside from the risk associated with cashflow issues, tenant behaviour was considered a key risk for many landlords. Landlords noted that bad tenant behaviour could derail their investment through:

- increased maintenance costs
- high tenant turnover
- legal costs associated with tenancy disputes.

Unsurprisingly, landlords expressed a preference for tenants with financial capacity and no propensity for property damage. While these landlords were sensitive to tenants' needs, they entered the property market for financial gain rather than to address social inequity. Therefore, schemes designed to entice them into affordable housing must provide confidence that appropriate tenants will be sought and make-good provisions enacted.

Make-good provisions guarantee that a property will be returned to the landlord in original condition at the end of a lease period. These agreements are important in headleasing. (Headleasing is when a housing agency rents private rental property from a landlord/owner and then on-lets that property to a tenant experiencing disadvantage.) Headleasing programs that include make-good provisions can incentivise investors to participate in affordable housing programs. However, such provisions can be expensive, costing on average $40,000 to restore a property to original condition. This means that headleasing can be a costly option.

Acquiring the funds to make good a property is challenging. Some community housing providers (CHPs) withhold a percentage of the rent to make good at the end of the lease, and others obtain funds from government subsidies—although these subsidy programs are viewed as grossly underfunded. While make-good provisions are costly, they represent an important opportunity to incentivise investors. Our survey showed that the average investor in our sample is 7 per cent more likely to participate in a scheme that offers make-good provisions than one that does not. Furthermore, the average investor would be willing to forego roughly $7,150 in annual tax rebates if a make-good provision was in place.

Affordable housing schemes

Our research found that 81 per cent of investors engaged in affordable housing schemes found them satisfactory, and between 40 and 60 per cent of respondents would be willing to participate in a scheme such as headleasing or the National Rental Affordability Scheme (NRAS). Despite this, only 39 per cent of small-scale investors in our sample were engaged in these schemes. Our qualitative research found that there were poor levels of awareness of affordable housing schemes. However, when investors became aware of such programs, they were interested in participating in them.

Furthermore, we found that the investment sophistication of long-term hold investors varies considerably; some are naïve and are negatively impacted by unexpected extrinsic financial changes that can cause them hardship. These investors present a risk to stability in the affordable housing sector. Due to lack of financial literacy, they may overcommit to their investment property, and experience financial hardship and be forced to sell the property when hit by unexpected extrinsic financial factors such as interest rate rises or extended periods without a tenant.

Headleasing

Focus groups and workshops with social housing providers, policy makers and small-scale landlords found that headleasing is an effective way to engage with small-scale private investors in the social and affordable housing ecosystem. Headleasing schemes avoid the need for major capital investment from CHPs and they increase and diversify the available affordable housing stock.

Headleasing is very attractive to private investors, but awareness of the option appears low among landlords. Landlords were unanimous in their support for headleasing schemes; most received market rent and were not exposed to risk. Benefits were fourfold:

- Guaranteed rental payments provided cashflow security—such rental guarantees made investors 12 per cent more likely to participate in a scheme.
- No loss of rent due to vacancy, and no need to advertise for new tenants.
- Guaranteed make-good provisions provided confidence that the property would be returned in original condition.
- Reduced administration demands when the property management was signed over to the social housing provider (SHP) provided peace of mind and a 'hands free' approach.

Regardless of these advantages, headleasing schemes do have drawbacks. In particular, landlords noted that indexing rents to market prices would increase their satisfaction with the scheme. As the schemes are designed to minimise landlord risk, they expose SHPs to considerable financial risk and are expensive to run. Headleasing schemes require an operating subsidy to meet the gap between market rent and social rent—which can be prohibitive for SHPs. Furthermore, while headleasing is viewed as popular, it is not suitable for tenants:

- with high needs
- escaping family and domestic abuse
- at high risk for property damage.

Small-scale investors

Small-scale investors present potential risks for affordable housing investment. Our qualitative engagement suggests that 'flippers', those who buy properties and quickly sell them for a profit, may create instability and inflate prices. However, it should be noted that our sample size was small. Similarly, investors engaged in short-let rentals through companies such as Airbnb inflate housing prices and create housing stress in areas with high tourist demand, especially in large inner-city urban areas in Melbourne and Sydney. Although flippers and short-let landlords are a relatively small cohort, they do have a negative impact on the affordable housing ecosystem. Long-term hold investors can also create instability if they face financial hardship. However, this only occurs in a small number of cases, and these investors are largely sensitive to tenants' needs and provide greater stability. For this reason, long-term hold investors are the preferred investors in the affordable housing landscape.

Community housing providers

Finally, our qualitative analysis found that CHPs were preferred over private investors due to the stability they provided and their capacity to mitigate the risks associated with private investment. However, CHPs do not have the capacity to invest in affordable housing at the scale required to address current and future predicted shortfalls. Therefore, long-hold private investors should be prioritised to meet demand and provide the quantity and diversity of housing stock that is required.

Policy development options

Who should be incentivised to provide affordable private rental housing?

All small-scale investment in affordable housing carries risks; these risks vary depending on the investor type.

Short-term hold investors often purchase higher-value properties with an intention to sell quickly at an inflated price ('flippers'). There is potential for these investors to inflate property prices and cause rental instability.

Long-term hold investors are more likely to provide stability and are therefore the more desirable target of government incentives. However, they also carry risk, primarily associated with a lack of financial knowledge; this can lead to failed investments and the need to sell the investment property in unplanned circumstances—especially because of extrinsic financial conditions such as interest rate rises.

Due to the risks associated with small-scale investors, it was noted that CHPs were the preferred target of government subsidies and programs. CHPs were seen to provide greater stability and fewer risk factors. However, CHPs do not have the capital capacity to provide an adequate supply of diverse affordable housing stock. Therefore, government policies aimed at incentivising long-term hold small-scale investors are preferred.

Incentivising small-scale investors through financial incentives

Long-term hold small-scale investors are incentivised by schemes that maximise the potential for a positive cashflow—not by financial schemes such as negative gearing and capital gains tax concessions. Our survey found that the average small-scale investor would need a tax offset of approximately $650 per year for every 1 per cent of market discount provided. These investors also value schemes that assure rental income, which underscores the importance of positive cashflow to this group. Furthermore, our qualitative analysis found that it is important to index rental increases to market rates so that investors who lock-in to long-term schemes are not disincentivised. Therefore, any programs designed to entice long-hold small-scale investors must prioritise incentives that support positive cashflow—for example, through rental guarantees and rents that are indexed to market rates.

Incentivising small-scale investors through make-good provisions

Make-good provisions provide landlords with confidence that their property will be returned to them in original condition at the end of the lease. Given landlords' concerns about social housing tenants, make-good provisions are a critical aspect of a social housing program that engages with the private rental market. Make-good provisions will incentivise landlords to participate in programs such as headleasing. However, make-good provisions are expensive, and acquiring the funds to make good a property is challenging. CHPs have the option to fund make-good provisions through retaining a portion of the rent or by obtaining government subsidies. Current government subsidy programs are grossly underfunded, and any such program should reflect that on average it will cost around $40,000 to make good a property at the end of the tenancy. Providing CHPs with access to adequate make-good funding subsidies will increase small-scale private investment in affordable housing.

Using effective communication and education programs to encourage appropriate investors

Low levels of awareness of schemes such as NRAS or headleasing has led to low levels of participation and affordable housing targets not being met. However, when small-scale investors do engage with affordable housing schemes, their satisfaction levels are high. A coordinated national marketing and education program targeting small-scale, LTHI to increase awareness of incentive schemes could improve participation in these schemes. Furthermore, our research found that if small-scale investors are not financially savvy, they can increase instability in the affordable housing sector, causing disruption for tenants. Education programs aimed at improving financial literacy among this group of investors could filter out vulnerable investors before they enter the affordable housing market, thereby minimising disruption caused by financial overcommitment. Adjusting prudential regulations could also support the goal of filtering out inappropriate investors.

Using headleasing to lure short-term lets into the affordable housing market

While media attention often focuses on the idea that short-term lets (STLs) on platforms such as Airbnb have a negative impact on housing, our research has shown that the impact of STLs is mainly in popular tourist destinations and some large inner-city urban areas, such as Melbourne and Sydney. That said, housing affordability is a significant concern in both tourist destinations and inner cities—especially for essential workers—and there is scope to incentivise small-scale investors in these problematic areas to move into the affordable private rental market.

Our policy workshop participants agreed that headleasing schemes that promote social and financial incentives have been successful in luring investors away from STLs in Tasmania. However, these schemes have had to provide broad-ranging and significant financial incentives addressing the rental gap, tenancy management fees and rental guarantees, as well as covering property damage. Despite the sizable costs of these schemes, they may be warranted in areas where short-lets create considerable housing stress. Our survey found that only 2.6 per cent of respondents favoured STLs as their most important investment strategy, and this suggests that a large proportion of small-scale investors could be drawn away from short-lets if the incentives meet their cashflow priorities.

The study

This project examined how governments at different jurisdictional levels can incentivise the provision of affordable rental housing by small-scale investors. Nearly one-third (31%) of Australian households rent their residential dwelling, and housing affordability is a particularly acute concern for low-income and middle-income households in the private rental sector (Australian Bureau of Statistics [ABS] 2021). Among other measures, governments have sought to address the issue by incentivising greater small-scale investment in the supply of affordable rental housing through the use of tax benefits, regulatory concessions and other policy levers. These efforts have had limited success, and incentivising small-scale investment in affordable private rental housing remains a challenge.

We reviewed national and international evidence on past and current affordable private rental housing schemes to identify factors that have contributed to their success or failure. We conducted qualitative interviews and focus groups with 40 small-scale investors and 10 asset managers across Australia to understand motivators for (and barriers to) small-scale investment in affordable rental housing. Furthermore, we undertook a nationwide online survey of 800 small-scale investors to quantify the marginal effect and relative importance of regulations, tax benefits and other policy levers that seek to design cost-effective incentives. Such incentives are intended to provide tangible and durable affordability benefits to encourage greater investment by small-scale investors in both regional areas and major cities, and to demonstrate economic and social payoff to governments. Finally, we held a workshop with nine policy makers to examine the efficacy and feasibility of different policy options.

Our research focussed on four research questions:

1. How have previous and existing affordable small-scale private rental housing schemes performed in Australia and internationally? What factors have contributed to their success or failure?
2. What are the motivators for and barriers to small-scale property investors investing in affordable rental housing?
3. What are the impacts of regulations, taxes, and other policy levers on small-scale investment in affordable rental housing?
4. How can governments at different jurisdictional levels incentivise the provision of affordable rental housing by small-scale investors?

This report synthesises findings from our analysis and identifies potential policy mechanisms that could be used to incentivise small-scale investment into the affordable private rental housing market. It includes specific policy recommendations directed at different levels of government.

1. Introduction

- **Nearly one-third (31%) of Australians rent their residential dwelling, and affordable rental options are becoming increasingly important to low-income and middle-income earners as they are being priced out of the market.**
- **Essential workers, older Australians and women are particularly facing housing stress, but even 'rich' households—with incomes over $140,000—are turning more and more to rental properties as the cost of buying a residential dwelling has become prohibitive.**
- **The shortfall of affordable and available private rentals hit 348,000 in 2021 for households with the lowest 20 per cent of incomes, and this shortfall is predicted to increase.**
- **Small-scale private investors comprise 90 per cent of all property investors in Australia. They own 23 per cent of all dwelling stock. However, government programs have had limited success in drawing these investors into the affordable housing market. For example, the National Rental Affordability Scheme achieved just over half of the targeted 50,000 new rental dwellings, leaving a significant shortfall.**
- **Given the low levels of affordable rental housing in Australia, and the moderate success of existing and previous programs at creating more affordable housing stock, it is important to find new, effective ways to incentivise small-scale investors to enter the affordable housing market.**

1.1 Background and policy context

Nearly one-third (31%) of Australian households rent their residential dwelling (ABS 2021). Affordable rental options are especially important for low-income and middle-income households in the private rental sector who are struggling to pay market rents (Rowley, James et al. 2016). The 2019–20 Survey of Income and Housing (SIH) found that 58 per cent of low-income households (the lowest 40 per cent of household income distribution) were spending more than 30 per cent of their incomes on housing (ABS 2019). The COVID-19 pandemic adversely impacted low-income and moderate-income households disproportionately, which further compromised their ability to afford private rental housing (Baker, Bloom et al. 2020; Oswald, Moore et al. 2020).

Evidence suggests that long-term structural change in the Australian private rental market, as well as short-term disruptions caused by the COVID-19 pandemic, have resulted in a shortfall in affordable private rental dwellings (Hulse, Reynolds et al. 2019; Gurran, Hulse et al. 2021).

Private rental was the fastest-growing sector of the housing system in Australia between 2001 and 2016, and the most acute shortfall of rental housing is impacting the lowest quintile household incomes (Q1), with 80 per cent of Q1 private renters paying unaffordable rents (Hulse, Reynolds et al. 2019). Although Hulse, Reynolds et al. (2019) reported a surplus of affordable housing for Q2 households, they also found that when this figure was adjusted for the availability impacts of higher income households, there was a shortfall of 305,000 dwellings that had been affordable for Q2 households in 2016.

Furthermore, Q2 households represent a critical sector of the workforce who face increasing difficulty in accessing affordable housing in the major urban centres where their work is located (Gurran, Hulse et al. 2021). These renters face acute shortages in the middle and inner urban areas that provide employment opportunities, with 71 per cent of renters in some urban areas paying unaffordable rent (Gurran, Hulse et al. 2021). More recent research has demonstrated that the lack of supply of affordable housing for low-income households has continued, with the shortfall of affordable rental properties for Q1 households reaching 255,000 in 2021—and when adjusted for utilisation by higher-income households, the shortfall increased to 348,000 dwellings (Reynolds, Parkinson et al. 2024). Post-COVID-19, the private rental sector in Australia has been characterised by 'rapidly increasing rents, very low vacancy rates and high levels of demand from migrants and additional households' (Reynolds, Parkinson et al. 2024: 2), and while the acute impact of the pandemic might be short-lived, the lack of supply of affordable housing appears to be an ongoing long-term trend.

Among other measures, governments have sought to address the issue by incentivising greater small-scale investment in the supply of affordable rental housing. For this study, small-scale property investors are defined as individuals or households—as opposed to companies, partnerships, trusts, funds, and not-for-profits—who own one or two investment properties. Small-scale investors comprise 90 per cent of all property investors in Australia and own approximately 23 per cent of all dwelling stock (Forbes 2021). Previous government schemes, such as the National Rental Affordability Scheme (NRAS), have tried to incentivise small-scale investment in affordable rental housing using different tax benefits, regulatory concessions and other policy levers. However, these schemes had limited success. For example, NRAS delivered 27,603 new rental dwellings by 2015, against an initial target of delivering 50,000 new dwellings by 2012 (Rowley, James et al. 2016). While many tenants receive rent assistance, there is little understanding of how this affects investment by small-scale landlords. Incentivising small-scale investment in affordable private rental housing remains a challenge.

1.2 Research questions

This project examines how small-scale property investors in Australia could be incentivised by different levels of government to invest in the supply and provision of affordable private rental housing. In particular, the project addresses the following four research questions.

1. How have previous and existing affordable small-scale private rental housing schemes performed in Australia and internationally? What factors have contributed to their success or failure?
2. What are the motivators for and barriers to small-scale property investors investing in affordable rental housing?
3. What are the impacts of regulations, taxes, and other policy levers on small-scale investment in affordable rental housing?
4. How can governments at different jurisdictional levels incentivise the provision of affordable rental housing by small-scale investors?

The study has developed specific policy recommendations directed at different levels of government on how they could best incentivise small-scale investment in the supply of affordable private rental housing within their jurisdictions.

1.3 Existing research

1.3.1 Affordable private rental housing in Australia

The private rental sector (PRS) is significant in Australia, as it comprises more than 26 per cent of housing (AIHW 2022; Hulse, Burke et al. 2012). The PRS is increasingly home to lower-income households unable to access social housing, and home to low- to middle-income households unable to enter homeownership because of housing price inflation. However, research on the PRS has tended to focus on the demand side of the market; the challenges facing both tenants (AHURI 2022) and home purchasers (Whelan, Pawson et al. 2023) and the housing assistance available to them are generally well understood. Far less is known about Australian landlords, their motivations, and how they respond to government incentives (and disincentives).

1.3.2 Small-scale investors

Private rental properties in Australia are primarily owned by small-scale investors who own on average one or a few rental properties (Wright and Yanotti 2019) in what has been referred to as a ‘cottage industry’ (Martin, Hulse et al. 2022; Longview PEXA 2023: 25). Institutional investment is very limited. This situation has been investigated to understand landlord motivations (see Beer 1999; Seeling 2009; Yates 1996).

Landlords can be either ‘purposeful’ or ‘accidental’. *Purposeful landlords*, or ‘landlord investors’, are those who have deliberately invested in residential property with the aim of leasing it. *Accidental landlords* come to landlordism accidentally—for example, upon inheritance (Beer 1999; Berry 2000; Morris, Hulse et al. 2021). A recent survey by Martin, Hulse et al. (2022) showed that 69 per cent of landlords acquired their rental property for investment purposes, while 26 per cent converted the property they had previously resided in into an investment property, with the remaining 5 per cent being accidental landlords. While most landlords rent out the entire property, some sublet a room (or rooms) in a house they occupy; such subletting landlords are often referred to as home sharers.

Morris, Hulse et al. (2021) argued that the dominance of small-scale investors can be attributed to a variety of factors. First, financial deregulation since the 1980s has led to the financialisaton of the housing market through new mortgage products aimed at rental investors, and tax settings have made rental housing an attractive investment for landlords—particularly negative gearing and capital gains tax (CGT). Landlord interest in rental housing in the 1980s and 1990s was motivated by negative gearing, rental income, and possible future income and capital gains (ABS 1998).

Seelig, Thompson et al. (2009: 2) found that landlords were not sophisticated and tended to invest from a place of 'sentimentality and informality' rather than an objective assessment of investment risk and return. More recent research suggests financial motivations have not changed, but that landlords are 'increasingly professionalised, hard-headed [with a] "financialised" landlord mindset' (Pawson and Martin 2021: 639). This mixture of motivations is consistent with some of the international literature (see for example Soaita, Searle et al. 2017). Despite financial motivations being a constant, Longview PEXA (2023) found that most landlords would be better off financially if they invested their money in superannuation, suggesting that private rental real estate investment is 'complex, stressful and risky' and assessment is beyond the average investor's capacity (Longview PEXA 2023: 1).

1.3.3 Who owns rental property in Australia?

Recent Australian Tax Office (ATO) data shows that of the 2.2 million individual investors with investment in rental property in Australia, 71.5 per cent own one property, 18.8 per cent own two properties, 5.8 per cent own 3 properties, 2.1 per cent own four properties and less than 2 per cent own five or more properties (see Table 1), demonstrating that the sector is dominated by very small-scale investors. It is important to note that this data is drawn from individual tax tenure and does not account for self-managed super funds (SMSFs), partnerships or companies.

Table 1: Rental property owners in Australia, number of properties owned, 2019–20

Number of rental properties	%
One rental property	71.5
Two rental properties	18.8
Three rental properties	5.8
Four rental properties	2.1
Five rental properties	0.9
Six or more rental properties	0.9

Source: ATO taxation statistics (2019–20).

Table 2 shows that there is a consistent level of investment across age cohorts from the age of 30.

Table 2: Rental property owners in Australia, number of properties owned, by age, 2019–20

Age range	Number of properties	%
Less than 30	96,704	4.3
30–39	455,227	20.4
40–49	550,462	24.7
50–59	571,927	25.7
60 or more	552,521	24.8

Source: ATO taxation statistics (2019–20).

The average rental property owner is a high-income, high-wealth household (Hulse, Reynolds et al. 2020), and many of them are increasing their portfolios to own multiple properties. According to ATO data, 29.4 per cent of rental property is owned by individuals in the top two tax income brackets, with another 32.6 per cent by the middle tax income bracket (see Table 3).

Table 3: Rental property owners in Australia, by taxable income range, 2019–20

Tax income group	Ownership of rental properties %
Less than $18,200	14.5
$18,200–$50,000	23.5
$50,001–$100,000	32.6
$100,001–$500,000	28.4
More than $500,000	1.0

Source: ATO taxation statistics (2019–20).

Investors turnover properties quickly, with 25 per cent of landlords leaving the sector within 12 months, and almost 60 per cent exiting—in other words, selling off their rental property—within five years (Wood and Ong 2010). This suggests evidence of capital-gains motivations for small-scale landlordism.

1.3.4 International examples of private rental sector small-scale investor incentives

In their analysis of the subsidised affordable rental housing sector in Australia, Rowley, James et al. (2016) examined various approaches that had been taken in other countries to incentivise private investment. We summarise their selected review of international examples below. Rowley, James et al. found that multiple strands of measures were implemented in Europe and North America: taxation credits, planning mechanisms, direct funding for development/redevelopment, government-based guarantees of housing debt, and tenancy agreements with landlords.

Rowley, James et al. concluded with two lessons that emerged from their review.

1. There is international evidence that over time a country can gradually develop a large, self-sustaining, affordable housing sector.
2. No country in their review was able to increase the supply of affordable housing exclusively through income support to households without using other resources to augment the subsidy scheme—such as public land or favourable planning mechanisms.

1.3.5 Summary

The private rental market is predominantly held by small-scale investors. Little is know about them. Being the largest stakeholder in the market, any attempts to incentivise the provision of affordable private rental housing must be undertaken with cognisance of the impact on and response of the small-scale investors.

However, existing schemes to incentivise the supply of affordable private rental housing have been disproportionately demand-side focussed, primarily through the provision of financial assistance. Housing assistance in its current form mitigates financial strain experienced by moderate-income to higher-income households, but is inadequate for low-income to moderate-income households (Stone, Parkinson et al. 2016). Rowley, James et al. (2016: 6) have noted that 'it is critical that government moves away from a reliance on demand-side subsidies that attempt to make housing more affordable for individual households, and instead sets in place supply-side alternatives'. This is because demand-side incentives do not necessarily engender supply-side participation.

It is crucial, therefore, to understand what motivates the dominant providers of rental housing—that is, small-scale investors—to shape policy interventions aimed at increasing their supply of affordable rental property. While some schemes identified here hold potential, such as headleasing and homesharing, little is understood about the way they should work in Australia to deliver optimal results.

1.4 Research methods

This project uses a mixed-methods approach to address four research questions, comprising both qualitative and quantitative analyses of different primary and secondary datasets. Project activities were conducted across four stages, corresponding to the four research questions. Table 4 summarises the four stages, their relation to the four research questions, and the methodologies for addressing each question. Over the following sections, we describe each stage in greater detail.

Table 4: Research questions, data sources and methodology

Research question	Data sources	Methodology (including data sources)
• How have previous and existing affordable private rental housing schemes performed in Australia and internationally? What factors have contributed to their success or failure?	State and federal government policy documents National and international academic research International grey literature and reviews 2019–20 Survey of Income and Housing	Review of previous literature Descriptive analysis of existing datasets
• What are the motivators for and barriers to individual households investing in affordable housing?	Qualitative interviews with 40 small-scale investors	Thematic analysis of semi-structured qualitative interviews
• What are the potential impacts on small-scale investors of changes in regulations, taxes, and other program infrastructure?	Online survey of 800 small-scale investors	Discrete choice experiments and analysis of investor preferences in affordable rental housing
• How can governments at different jurisdictional levels incentivise the provision of affordable housing by small-scale investors?	Policy workshop/focus group (online)	Policy analysis and synthesis Policy workshop/focus group (online)

Source: Authors

Stage 1: Review and secondary analysis

Stage 1 reviewed evidence on affordable private rental housing schemes that operate (or have operated) in Australia and internationally. The review included key assistance measures delivered by the federal, state and territory governments:

- the National Affordable Housing Agreement (NAHA)
- Commonwealth Rent Assistance (CRA)
- Private Rent Assistance (PRA)
- National Rental Affordability Scheme (NRAS; now discontinued).

We also reviewed other more targeted Australian schemes, such as Defence Housing Australia (Phibbs and Hanna 2010), the HomeGround Real Estate Scheme, and headleasing schemes. Finally, we reviewed Australian schemes that could have indirect implications for small-scale investment in affordable rental housing, such as the First Homeowners Grant (FHOG) and Private Rental Brokerage programs (PRBPs) (Tually, Slatter et al. 2016). International examples include the Low Income Housing Tax Credit scheme (US), and the Housing for Rent schemes (UK).

We assessed the performance of different schemes in terms of their:

- ability to provide affordability benefits to households in greatest need
- demonstrable economic and social returns to governments investing in them
- investment benefits to participating small-scale property investors.

We examined the different factors that have contributed to the schemes' success or failure, such as financial incentives and tax benefits, planning concessions or obligations, tenancy requirements, management and administration, and relationships between real-estate developers, property agents, small-scale investors and other actors.

Stage 1 also comprised secondary analysis of existing datasets. The 2019–20 ABS Survey of Income and Housing (SIH) was used to build a profile of households investing in rental housing, alongside income and tax data collected by the ATO. We undertook a cross-tabulated descriptive analysis of these datasets to examine how investment in rental housing properties (value of rental property, equity in rental housing, rental housing loan amounts, number of rental properties owned, relationship with any co-owner in the rental property, and the rental income) has varied as a function of investor household attributes (age, income, wealth, location). Similarly, the 2021 ABS Census and Australian Property Monitors' point level dataset was used to examine how affordable rental housing supply has varied across different spatial submarkets, and to identify potential factors that have contributed to these differences.

Stage 2: Qualitative engagement with small-scale investors and asset managers

Stage 2 examined motivators for and barriers to investment in affordable rental housing by small-scale investors. We interviewed 30 small-scale investors, stratified geographically (10 metropolitan and five regional each from Victoria and South Australia) and demographically (based on the profiles generated by our secondary analysis in Stage 1). The sample was recruited through Focus People Pty Ltd, a market research company that has been used before by Report author Lowies for similar work. All interviews were conducted online. Interviews were recorded and transcribed using AI transcription services.

We undertook additional engagement with landlords and tenants who have participated in headleasing schemes. While most schemes use financial incentives, risk and reward undergoes a shift when headleasing is involved (Sharam, Byford et al. 2018), which suggests that different factors might be at play for headleasing schemes. Therefore, we undertook one focus group with 10 investors who have participated in headleasing schemes to understand the landlords' perspective, and one focus group with 10 asset managers from state housing authorities and CHPs that have offered headleasing schemes to understand the lessors' perspective. Both focus groups were conducted online. Report author Sharam has extensive social-housing asset management contacts and recruited participants for both focus groups through her networks.

While the sample sizes for the qualitative engagement were small, we used the findings from the interviews to shape the quantitative engagement and used the findings from the focus groups to contextualise findings from the survey.

Stage 3: Stated preference survey of small-scale investors

Stage 3 focussed on the impacts of regulations, taxes and other attributes on small-scale investor preferences for participation in affordable rental housing schemes. We used an online stated preference (SP) survey to measure these preferences. SP experiments can be used to quantify the marginal effects of different scheme-specific attributes on investor participation, identify the relative importance of each attribute, and predict investor participation rates for different future schemes, including those that vary substantially from historic schemes trialled previously.

We recruited a panel of 800 small-scale investors from across Australia to participate in the online survey. The sample was recruited through the market research company PureProfile. Report authors Vij and Ardeshiri have used this company to conduct similar data collection exercises. In 2021, they used PureProfile to recruit 3,000 demographically and geographically representative individuals across Australia for an online survey to elicit preferences for regional living. In each of their previous experiences with the company, they have been very satisfied with both the representativeness of the sample and the quality of the responses.

The online survey presented participating investors with multiple SP scenarios where they were offered the choice to invest in two or more competing affordable rental housing schemes that differed in terms of tenancy eligibility, leasing periods, management fees, financial incentives, and other relevant attributes identified by previous stages. For each scenario, participants were asked to indicate their most preferred option. The SP experiment design was informed by findings from Stage 1 and Stage 2. Alternative attributes were systematically manipulated across scenarios to understand how small-scale investors value each of these attributes. Additional information relating to investor demographics and attitudes was also elicited. The data collected was used to estimate the marginal effects of regulations, taxes and other attributes on small-scale investor preferences for participation in affordable rental housing schemes.

Stage 4: Policy analysis and synthesis

Stage 4 examined how governments at different jurisdictional levels can incentivise the provision of affordable rental housing by small-scale investors.

This stage comprised an online workshop with policy makers who were representatives from the Commonwealth Treasury and Department of Social Services, and state government housing departments. We included nine representatives, from New South Wales, Victoria, Queensland, South Australia and Western Australia. The research team worked with AHURI to finalise workshop participants. A confidential draft summary of the research findings and policy options was provided to policy makers prior to the workshop to enable a review of the efficacy of the schemes explored and the feasibility of future policy options. The workshop explored these issues further.

Findings from the workshop have been synthesised with findings from stages 1–3, with the aim of developing specific policy recommendations for different levels of government on how best to incentivise small-scale investment in affordable rental housing. In particular, our analysis and synthesis identified cost-effective incentives that provide tangible and durable affordability benefits to encourage greater investment by small-scale investors—in both regional areas and major cities—and to demonstrate economic and social payoff to governments.

2. Headleasing

- **Headleasing is used extensively to provide social and affordable housing.**
- **A key advantage of headleasing is that it avoids the need for major capital investment by private investors.**
- **Headleasing is very attractive to some private investors, but awareness of the option appears to be low among landlords.**
- **Market conditions impact on the availability of housing for headleasing.**
- **Lack of subsidies to address the gap between social and market rents and for make-good provisions limit the extent of headleasing.**

2.1 Literature review

Headleasing involves the leasing of private rental accommodation by state housing authorities or CHPs, who then sublease these properties to approved households—usually social housing tenants. Headleasing is a form of non-owned strategic asset management. It is flexible and does not require upfront capital expenditure—although make-good provisions may require capital expenditure at exit. Headleasing is an option:

- when an SHP does not have the type of housing required in its portfolio—for example, five-bedroom homes
- when there are special physical accessibility or security needs
- to overcome discrimination in the market
- when a tenant does not have a rental history.

A headleasing arrangement generates two separate leases on each property:

- a lease between the landlord and the government agency/CHP
- a lease between the tenant and the government agency/CHP.

This arrangement provides security of income to the landlord for a defined period of time, while also providing access to rental housing to households that would otherwise have struggled to access housing on the open market. A market rent is paid to the property owner by the state housing authority or CHP, while the tenant pays a market, social or affordable rent to their social landlord. Examples of current headleasing programs in Australia are the DCJ Headleasing Program in New South Wales, the Helping Hand Headlease Scheme in Queensland, and the Victorian Government Headleasing Program. Little is currently understood about Australian headleasing schemes.

Internationally, Winters and Van den Broeck (2022) noted that headleasing has gained considerable favour in recent years in the face of declining social housing funding. De Decker (2012), Hegedüs, Horváth et al. (2014), Lalor (2014), Pareja-Eastaway and Sanchez-Martınez (2017), and Archer, Crisp et al. (2019) suggest that headleasing is a positive option.

However, Winters and Van den Broeck (2022: 607) argue that 'no studies have rigorously investigated the costs, nor the cost-effectivity' of headleasing. Their study investigated social rental agencies (SRAs) in Flanders. Flemish SRAs headlease private stock; they emerged in the 1990s in response to the constrained housing options for households that were eligible for social housing but unable to access it. Like Australia, Flanders has a low proportion of social housing with low-income and vulnerable households making up a significant group of private rental tenants. Flemish private rental stock is more likely to be older than social housing.

In 2018, there were 48 SRAs who headleased 10,990 dwellings. The SRAs received operational subsidies from government, and tenants may receive rental support. Headlease rents are market-based, adjusted for risk—the rental payment guarantee and a make-good provision effectively results in a discount to market of 17.4 per cent. In contrast, the rental guarantee in Ireland attracts an 8–12 per cent rent discount for the same guarantees, although the lease duration is between one and four years (Hegedüs, Horváth et al. 2014). Flemish homeowners qualify for a reduced VAT rate on renovations and discounts on property tax, and some municipalities offer other incentives. Headleases are of limited duration, but are for a minimum of nine years. Winters and Van den Broeck (2022) compared the costs and cost-effectiveness of SRAs to social housing. They found that the SRA scheme is more expensive for governments than social housing. This was largely because the SRA subsidies are operating costs that do not provide any asset ownership—unlike social housing. De Decker's earlier evaluation of the Flemish SRAs indicated a very high level of landlord support (De Decker 2009), which suggests that the risk-adjusted return on investment is attractive.

Another notable finding by Winters and Van den Broeck (2022) is that the SRA housing only met energy standards in 35 per cent of cases. This is likely to correlate to the age of the stock, and points to the problem of low-quality housing contributing to high living costs. Recognising this issue, an SRA run in Catalonia, Spain, provides private owners with renovation subsidies of up 6,000 euro per property to ensure properties meet rental standards (Archer, Crisp et al. 2019).

2.2 Focus groups

Two focus groups were conducted, one with eight SHPs, and another with nine small-scale landlords who lease their properties to SHPs. Each focus group was asked a range of questions regarding motivations; advantages and disadvantages; risks; insurance; impact of market conditions; legal issues; maintenance and asset management; impact on the liquidity of investment; and tenants.

2.2.1 Investors

Most of the landlords became aware of the headleasing option when their property managers indicated that a SHP was interested in their property. Two had purchased property subject to existing contracts. They did not understand why the option is not promoted: *'[The SHP] approached the agent and … I was like, Wow, I never heard of this'* (Participant 1).

The landlords were unanimous in their support for headlease programs, and indicated they would put any subsequent property they purchased into a headlease scheme. Mostly they received market rent and took no risk. In general, they were not anxious to increase rents as soon as possible when market rent increased—which indicates that headleasing insulates landlords from rental price downturns. The advantages for landlords included the following:

- Guaranteed rental payment. While market rent was desirable, the guarantee of rental payment was far more important: *'Rent is always paid on time, so there's no issues with rent, there's no issues with the money coming through, or bills'* (Participant 4). In landlords' experience, rents move down as well as up; increasing rents tends to promote tenant mobility, which imposes other costs, including re-tenanting properties and the potential for non-payment.
- Headleasing guarantees rental income, so there is no loss of income when there is a vacancy. Headleasing also removes the need to advertise for new tenants:

> *When you're renting on the private market … tenants leave every 12 months or so, and then you've got to pay the re-advertised costs and the re-letting costs … It's a bit of a hassle, and it just not really worth [it]. (Participant 3)*

- Maintenance and make-good provisions. While tenancy legislation requires that properties be returned in the same condition, less reasonable wear and tear, SHPs guarantee this outcome and assume the liability if the tenant does not pay for damage. Further, landlords can enter an arrangement with the SHP to provide maintenance throughout the tenancy. SHPs have their own contractors, who are reliable and on-call. Some of the landlords were very happy not to have to chase tradespeople to get work done: '*[The contract says] they're going to return it to the original state … That is peace of mind for me … even if they pay slightly lower rent … it's worth it'* (Participant 1).
- Reduced administration. Participant 4 argued that headleasing meant the investment took *'care of itself'*. While some landlords retained their property manager—generally because of existing contracts with them—management could also be signed over to the SHP. In effect, it provides the opportunity to 'set and forget'.

The headlease terms were generally short. There are several government programs that encourage CHPs to headlease properties. Some limit the capacity of the CHP to enter into longer leases—probably because the funding is not guaranteed. The landlords were very keen to have longer leases. For example, Participant 4 noted: *'I would love a longer lease term … Having peace of mind.'* Participant 3 noted: *'I'll be willing to push [the lease] to five years if there's really good tenants and maybe even longer than that.'*

Most of the landlords, supported long leases because they cared about their tenant: *'We're kind of invested in the tenants now a little bit and we feel you know, where are they going to live because that's their home.'* (Participant 6) These landlords had also had varied past experience with tenants, and some admitted a preference for tenants they perceived as low-risk. However, none indicated they had sought to direct the SHP on whom they could house. As Participant 4 argued:

> *[Tenants are] going to trash their places, and they're going to do whatever they're going to do. But the end of the day, [the property is] actually going to get fixed as well. It's going to get maintained. (Participant 4)*

The landlords' experiences of the make-good clause in their contracts provided the comfort required to overcome the anxiety that social housing tenants may be risky. Participants 7 and 8 suggested that many areas where there was high demand for private rental housing were characterised by low socio-economic groups that are much like social housing tenants: *'[I'd] rather be backed by … some social housing [organisation]'* (Participant 7). Participant 7 said his property was in an area with a high proportion of recent migrants and he had found it hard to overcome communication and language barriers, and this was something that SHPs are good at.

Asked about how governments could incentivise headleasing, the landlords' primary response was to ask why governments did not promote awareness. A Victorian landlord felt the increase in land tax would be a disincentive for landlords who own inner-city properties, and suggested a discount on land tax in cases where the tenant is a low-income essential services (key) worker:

> *'We've got one of the [older] women. She does do some casual work at the [deleted] Hospital for cleaning… so she needs to live in the inner-city area, but the land tax…is so expensive.' (Participant 2)*

2.2.2 Social housing providers

The primary reason for SHPs headleasing private properties was to grow stock in the absence of capital (Participants 9, 10), but it also meant obtaining properties in locations that are prohibitive from a capital perspective (Participant 11) or which allowed tenants to be located away from existing concentrations of social housing (Participant 12).

SHPs understand the key advantage for investors is guaranteed rental income and reduction of risk (Participants 9, 11, 12). Another advantage is providing a market for hard-to-let properties. Participant 9 argued:

> *We win [landlords] over because we're out there getting … what would be considered hard-to-let properties. And so we're getting properties that are already not exactly necessarily up to standard. (Participant 9)*

The SHPs assume significant risk in providing guarantees. However, investors and real estate agencies—which are effectively the conduit to property owners—are wary of headleasing because of the public perception of social housing tenants. The stigma is significant, and several SHPs said that knowledge of a single bad experience with a tenant quickly destroyed agent and landlord interest even if there were no problems in 99 per cent of cases (Participants 12, 13, 14). This was especially the case for mum and dad investors. However, many SHPs had been successful in developing relationships with investors who came back with additional properties (Participant 15).

Once real estate agents know SHPs will provide ongoing support to tenants, they are far more likely to seriously consider the option: *'[They understand we are] not just going to dump them in there and they're on their own'* (Participant 13). Indeed, Participant 13 indicated this support enabled the SHP to obtain lower rents.

A key issue for SHPs is attracting the right type of investor. The ideal investor:

- is not emotionally engaged with their property
- does not feel the need to maintain active involvement.

These 'set and forget' investors are comfortable having a passive, secure investment (Participant 11). But many investors are not so detached and require management, which adds to overhead costs (Participant 9). Almost all properties are obtained via real estate agents; these agents generally have contracts with the landlord and sometimes feel the need to maintain an active role in monitoring the property and the tenant, even though this also adds to overhead costs (Participant 10). Some SHPs preferred to contract directly with owners, thus saving the owners the agent fee, although Participant 9 said that could be problematic. Others said the presence of an agent was more likely to mean the owner would 'set and forget'. Where the SHP had a large number of headleases, management systems become critical. Participant 12 said it had been challenging to introduce new management software that worked for both parties, and that real estate agents were far more likely to have standard software skills than investors.

Lease terms

The lease term has implications for whom the SHP houses (see 'Choice of tenant' below) but also for:

- transaction costs
- maintenance regimes (where the SHP takes responsibility for it)
- make-good provisions.

Most of the headleasing appears to be for short periods—for example, 12 months to three years (Participants 9, 12). This reflects government programs aimed at rapid housing in the case of domestic and family violence, or for transitioning tenants into private rental. CHPs' headleasing largely reflected the incentives provided by government programs. There was a strong preference across the board for much longer lease terms, as this would align the needs of tenants, asset management and administration.

While headleasing provides the opportunity to obtain property without capital investment, a capital subsidy is often required for make-good provisions (see next section) and an operating subsidy is required to meet the gap between market rent and social rent (Participant 11). Some government programs for specific tenant cohorts provide an operating subsidy, but these tend to be for short-term leases. A 20-year headlease will involve a formula for rent increases. In order to attract investors into long-term headlease schemes, rents cannot fall too far behind market rents. The SHP not only needs to fund the discrepancy between market rent and social rent, it also needs to consider the impact of a change in tenant, as social rents are reflective of household income. The SHPs considered 10-year leases as desirable, and recognised that longer leases should be the basis of a 'set and forget' investment model (see 'Future schemes' below).

For SHPs, a disadvantage of short-lease periods is when investors fail to renew leases when market conditions mean they can do better outside a scheme (Participant 12)—for example, escalating costs or high market rents. Current market conditions had resulted in an unprecedented number of investors selling properties. Given that lease periods are often short, the existence of a headlease does not unduly restrict the market for potential buyers—unlike a very long lease. And although a landlord's ability to sell a property is fundamental, ensuring investment liquidity, property sales are disruptive for tenants (Participant 9).

Maintenance and make-good provisions

Make-good provisions were a critical issue for investors and SHPs. The make-good provisions ensure a property is returned in the same condition as when it was let, minus reasonable wear and tear. Detailed property-condition reports are vital and are the basis for the transparency (Participant 10). The SHP must have very good asset-management systems and personnel, with headleased properties treated identically to owned assets (Participant 11). Not doing so means the assets cost 'a lot of money' (Participant 9). Asset management becomes even more important with hard-to-let properties, as these tend to be in poor condition and are more costly to maintain. The *'property condition at the outset is critical, because we don't want to be lumbered with embedded maintenance liabilities'* (Participant 11).

Make-good costs can be very high. Specific tenant cohorts, such as those who have been involved in the juvenile justice system, typically incur greater damage. Participant 14 said they often spent $25,000 to $50,000 on restoring each property. However, governments do not fund CHPs for make-good provisions, or these provisions are grossly underfunded: *'We're not funded for anything more than $150 per property which is … not even a letterbox that's been stolen'* (Participant 9).

Some properties also require modifications, such as for disability accessibility, and these need to be removed at lease expiry (Participant 9).

Choice of tenant

Headleasing was not regarded as suitable for all tenants, with a distinction being drawn between *'eligibility and suitability'* (Participant 14). Difficult tenants, such as those with significant mental health or alcohol and drug issues, require active tenancy management, and may also incur greater property damage. CHPs without adequate funding are required to find internal funds to cross-subsidise such tenants, and this limits how many people they can house via headleasing. More importantly, the reputation of headleasing programs is put at risk.

Most headleased properties are for a very short duration. Knowing the house can be taken away *'causes a lot of distress to tenant[s]'* (Participant 9). The short-term nature of much headleasing was regarded as a very poor method of supporting those escaping domestic and family violence.

Some government-funded programs aim at transitioning tenants into private rental arrangements, but many tenants cannot be *'successfully supported … and need to be relocated into permanent social housing'* (Participant 9). Where tenants are transferred from permanent social housing to a headleased property, issues such as pets become problematic if the investor does not allow a pet.

Landlord insurance

A perceived barrier to headleasing was the availability and/or cost of landlord insurance. Landlord insurance may not be available for sublet properties, or may be more expensive when letting to a SHP (Participant 9). However, as Participant 12 noted, it is unnecessary for investors to have landlord insurance because the SHP guarantees rental payment and is obliged to make good.

Future schemes

Headleasing was viewed by the SHPs as an important method of obtaining properties with relatively little capital outlay. For CHPs, the key deficiencies were the lack of capital subsidy for make-good provisions and the lack of an operating subsidy to meet the gap between social rents and market rents. For SHPs, guidance on acceptable market rent did not account for price inflation; they also found allowable lease terms were too short. Many had explored how schemes could be more attractive to investors.

Participant 11 said their organisation was looking at a build-to-sell, lease-back model similar to the Defence Housing model. They were investigating how discounted rent could become a charitable donation for taxation purposes. This model generates a developer margin that can be used to subsidise the headleases. However, it does require having access to capital.

The SHPs suggested there was a need to align residential tenancy legislation and other legislation concerning headleasing (Participants 10, 11).

The SHPs proposed a comprehensive national scheme that would aggregate investment: *'Instead of everyone going individually, it's under a banner of some sort. BlackRock is managing my investments,'* said Participant 11. This scheme should appeal to 'set and forget' investors, as it offers long-term value.

> *One of the major keys to unlocking access to private investors' properties is long-term projects, not three years, six months [or] five years. Twenty years, that sort of thing, to provide long-term stability. (Participant 11)*

SHPs suggested a new single national scheme or platform that would provide a conduit to investors, and be a means to educate investors: *'It's almost a marketing exercise … in terms of telling investors that this is a good form of investment'* (Participant 10).

Such a platform could advise investors where investment was needed (Participant 10). Key to such a scheme would be a commitment by government that they would provide a subsidy to address the gap between social rents and market rents.

The issue of scale is already being addressed by impact-investor intermediary Conscious Investment Management (CIM), which has partnered with the CHPs Haven Home Safe, Housing First and Bridge Housing. In each case, CIM purchases properties—150 units in one case—and headleases them to the CHP for 10 years. The CHP manages the property as well as the tenant. The scale reduces transaction costs when compared to dealing with numerous individual landlords. In each case, the headleasing is underpinned by state government programs that provide a dedicated subsidy stream to support social housing tenants.

2.3 Policy development implications

Headleasing is a means by which private investment in housing can be utilised for social and affordable housing. With the right policy settings, it could deliver a pool of relatively long-term social and affordable housing.

There are private investors for whom the model is very attractive—but in general, there appears to be a low level of awareness of headleasing among landlords. This suggests that marketing efforts need to be improved. The scale of housing need and constraints upon public capital investment suggest that a more coordinated, national approach to headleasing using, for example, an aggregator model, would be valuable.

Additional incentives may be required to increase the scale of headleasing. Any new incentives should appeal to investors' cashflow considerations to encourage property as a passive long-term investment.

Headleasing is attractive to SHPs as it has the advantages of flexibility and minimal capital expenditure. However, headleasing is limited by the lack of subsidies required to address the gap between social and market rents and to provide for make-good provisions. Lack of subsidises and stigma, to some extent, mean that SHPs are overly reliant on poor quality stock—which has implications for tenant wellbeing and increases maintenance outlays.

3. Investor motivations and incentives

- **Small-scale landlords are a mixture of purposeful and accidental landlords.**
- **The largest group are described as *long-term hold investors* (LTHIs). They are moderate-income households that invest on the basis of being positively geared, which means they are cashflow-sensitive. They aim to build wealth for retirement or for their children.**
- **A much smaller group are described as *short-term hold for capital gain investors* (STHCGIs). These are high-income households that use interest-only loans, are negatively geared, and rely on capital appreciation to create wealth.**
- **The investment sophistication of LTHIs varies considerably. In general, they purchase cheaper housing and are sensitive to the affordability issues faced by tenants.**
- **STHCGIs regularly flip properties, which creates insecurity for tenants. They buy property with low-maintenance demands.**
- **Tenant behaviour is a key property investment risk.**

3.1 Existing schemes to incentivise small-scale investors

Multiple government interventions have directly or indirectly targeted landlords in a bid to incentivise increased participation in the affordable private rental market. The main levers are tax subsidies, other financial incentives, demand-side supports, capital grants and planning policies (see Rowley, James et al. 2016).

3.1.1 Tax concessions

Tax incentives are a significant policy lever used by governments. The following concessions are applicable to small-scale investors.

- **Capital gains tax (CGT) discount:** CGT is the tax individuals pay on the capital appreciation on a property obtained at subsequent sale (ATO 2022). A 50 per cent discount on CGT was introduced in 1999 for property held for at least 12 months. (Prior to this, the capital gain was indexed to the consumer price index to avoid taxing gain acquired because of inflation.) There is an additional CGT discount of up to 10 per cent for individuals who provide affordable rental housing to low- to moderate-income households, bringing the discount up to 60 per cent. This extra incentive was introduced in 2018, and the property must have provided affordable housing for a minimum of three years and been managed by a registered community housing provider (CHP). Recent estimates show that the major beneficiaries of CGT discounts are high-income earners, with nearly 91 per cent of the total CGT benefit received by individuals with an above-median taxable income, and 75 per cent by the top 10 per cent of income-earning individuals (Treasury 2023).
- **Depreciation allowance:** The depreciation allowance allows rental property owners to claim the decline in value of depreciating assets as a deduction against their personal income tax, thus reducing their overall tax burden.
- **Negative gearing:** Negative gearing permits the investor to claim losses associated with owning and leasing the property as tax deductions against their personal tax and any other income tax. Costs include interest on loans, and losses can be carried forward to the following income year (ATO 2022). High-income earners are the major beneficiaries of negative gearing (Morris, Hulse et al. 2021). Some estimates indicate that more than half of the benefits of negative gearing are enjoyed by the top 10 per cent of income earners, while only 6 per cent of the benefits go to the bottom 20 per cent of income-earning households (Grudnoff 2015). Negative gearing remains a 'hook' that lures investors into the private rental sector (Hulse, Burke et al. 2012: 18).
- **Tax rebate (NRAS):** The National Rental Affordability Scheme (NRAS) was a federal assistance measure introduced in 2008 in conjunction with state and territory governments to 'increase the supply of affordable housing, reduce rental income for low to moderate income households and to encourage large scale investment and innovative management of affordable housing' (Department of Social Services 2022). Modelled after the Low-Income Housing Tax Credit (LIHTC) program in the US, it offered an annual tax rebate for a period of 10 years to investors who built new housing and offered it at 20 per cent below market rent to low- to middle-income earners. The rebate was set at $10,000 per annum and indexed (amounting to over $11,000 per dwelling in 2023–24). The NRAS scheme was discontinued in the 2014–15 Federal Budget, and all existing incentives are due to expire by 2026. In total, the NRAS delivered 36,218 properties, although only 24,038 properties remain in the scheme as many incentives have already expired. There are 348 provisional allocations for dwellings yet to be delivered (Department of Social Services 2023b).
- **Land tax exemption:** In the ACT, there is a full land tax exemption for private property owners who rent their property through a 'registered community housing provider for affordable community housing purposes' (ACT Revenue Office 2023) at a minimum discount to market of 25 per cent to tenants with a combined annual gross income of less than $100,000.
- **Charitable tax deductions:** Social enterprise real estate agencies such as Homeground have been provided with a private tax ruling, which means the rent foregone by landlords who accept submarket rents can be claimable as a tax-deductible donation, hence reducing investors' assessable income (Homeground Real Estate Canberra 2023).

Recent research indicates housing offered to the short-let markets (such as Airbnb) comes at the expense of the long-let market (Martin, Hulse et al. 2022). This trend has led to attempts by governments around the world to boost rental housing supply by discouraging short-term lets (STL) through taxation, among other levers. In Australia, the CGT discount that applies to rental property cannot be claimed for short-term rentals. However, there is very little taxation disincentive to STL in Australia beyond this tax difference, with calls being made and refuted in multiple quarters about the potential of an 'Airbnb tax' to influence the private rental market. In Victoria, for example, it is currently being mooted that an additional tax should be placed on short-term rentals in response to the ongoing low levels of affordable rental housing (Carmody 2023).

3.1.2 Financial regulation

Investors' decisions are impacted by prudential regulation of the banking sector, aimed at mitigating the risk of financial instability arising from excessive housing price inflation. In the aftermath of the Global Financial Crisis, the Australian Prudential Regulatory Authority (APRA) departed from its previous equal treatment of owner-occupiers and housing investors (APRA 2019) to counter the growth of high-risk lending (Martin, Hulse et al. 2022). The resultant measures led to decreased levels of investor borrowing which, by extension, lowered the supply of new housing, among other effects. This targeted dampening of investor lending was initiated in 2014 and ran until the 2020s despite the withdrawal of the disincentivising measures in 2018. At present, increasing the Reserve Bank of Australia (RBA) cash rate in response to high inflation has a knock-on effect. It reduces investor borrowing as debt becomes more expensive, which leads to lower new supply and higher house prices, which then drives rents up as landlords pass on the cost to renters.

3.1.3 Demand-side assistance

An indirect channel through which private investment in the PRS is supported is through subsidising rental payments and provision of other types of housing assistance. A suite of programs across federal, state and territory governments target private renters (Stone, Parkinson et al. 2016). These are outlined below.

- **Commonwealth Rent Assistance (CRA):** CRA is a non-taxable assistance payment paid (mostly fortnightly) to eligible recipients who rent in the private rental market or in community housing. It was established with the aim of supporting low-income earners, and is relatively well targeted (Productivity Commission 2019). CRA is paid at 75 cents per dollar above a minimum rental threshold until a maximum rate is reached, with the latter varying based on household or family situation (Department of Social Services 2023a). The most recent estimates show that as of June 2021, around 1.5 million beneficiaries were receiving CRA, to the tune of $138 per fortnight per recipient, equivalent to 2 per cent of median fortnightly rent (AIHW 2022). CRA remains the most significant form of housing assistance available to Australian households (Productivity Commission 2019), with 2020–21 government real expenditure on CRA totalling $5.3 billion (Steering Committee for the Review of Government Service Provision [SCRGSP] 2022). The 2023 federal budget increased the CRA rate by 15 per cent over five years; the 2024 budget added a further 10 per cent increase, representing the first back-to-back increase in the maximum rates of CRA in thirty years.
- **State private rent assistance:** States and territories also provide different types of private rent assistance payments. These payments target households that are experiencing difficulty in securing or maintaining private rental housing (AIHW 2022; Productivity Commission 2019). Administered under the National Affordable Housing Agreement (NAHA), these are usually one-off forms of financial support, but can include ongoing rental subsidies and payment of relocation expenses. Private rental assistance (PRA) was provided to almost 63,000 unique households in 2020–21, the lowest since 2013–14, and following a general trend of decline from 160,000 households in 2010–11 (AIHW 2022; Productivity Commission 2019). Some of the most common types of PRA are outlined below.
    - **Bond loans:** All state and territory governments provide interest-free loans to eligible low-income households that are unable to pay their rental bond. The average bond loan amount beneficiaries received across all states and territories in 2020–21 was $1,216 (AIHW 2022). Some states require the bonds to be paid back at the end of the tenancy, while others require immediate repayment by instalments.

- **Advance rent:** These are one-off rental grants to support eligible households to start or maintain their rental tenancies. These grants are paid in New South Wales, Queensland, South Australia and Tasmania. In 2020–21, there were about 23,702 households receiving one-off rental grants across the four states, at an average of $512 (AIHW 2022). In Victoria, this advance rent is in the form of the first month's rent paid to support individuals or households who are at risk of or experiencing homelessness, among other eligibility requirements.
- **Relocation assistance:** This is financial assistance offered to eligible renters to assist them with the costs associated with establishing a new private rental tenancy, such as connection of utilities and removalist expenses. The average relocation assistance given across the states and territories in 2020–21 was $1,824, a 10-fold increase relative to $180 in 2013–14 (AIHW 2022).
- **Tenancy guarantees:** Some state housing authorities support eligible tenants with limited or poor rental history to secure private rental housing by providing landlords or their agents with a formal guarantee to cover the potential future rent arrears or property damage over and above the rental bond. Examples include the Housing NSW Tenancy Guarantees and the Western Australian Rental Pathways Scheme.
- **Private tenancy facilitation:** A range of services provided by state governments to prepare prospective or existing renters for their tenancy. It includes education on renters' rights and responsibilities, conducting property searches, preparing and submitting relevant documentation, and liaison with property owners and their real estate agents.
- **Private rental subsidies:** These are regular or time-bound subsidies aimed at financing a portion of rents for eligible tenants. In Victoria, the Private Rental Assistance Program (PRAP) provides private rental subsidies to support financially disadvantaged households and/or victims of family violence to maintain or secure private rental tenancies. In New South Wales, Rent Choice subsidies support access to safe and affordable private rental housing to residents who have endured a major financial setback or are escaping family violence, are war veterans, or youth. These subsidies provide medium-term financial assistance for up to three years to eligible low- to moderate-income households by paying the difference between the market rent and the household's affordable rent, calculated as a percentage of their gross assessable income.
- **Private rental brokerage programs (PRBPs):** While CRA and PRA support tenants by lowering housing-related stress, PRBPs 'aim to help the clients themselves, usually through advice, information, introductions and timely support, in order that they can compete successfully for rental properties in a competitive market and sustain their tenancies over the longer term' (Tually, Slatter et al. 2016: 22).
- **Arrears assistance:** This is an interest-free loan or grant accessible to eligible tenants at risk of eviction due to rent arrears. This is usually in the form of emergency financial assistance to pay off rent arrears when tenants face extreme unforeseen circumstances that place them at the risk of eviction. For example, in Victoria, eligible renters can receive a one-off payment towards rental arrears through the PRAP.
- **Key worker affordable rentals:** Generally, key worker affordable rentals consist of rental housing targeted at key workers. Such housing is let out at submarket prices to increase affordability for key workers. Key workers in Australia include 'teachers, nurses, police and fire and emergency personnel … workers across the broader public sectors, support/ancillary workers in healthcare, education and emergency services, workers who support the labour force (e.g. childcare and aged care workers and ICT support professionals and technicians) and low-paid workers who are important for local economies, such as hospitality and retail workers' (Gilbert, Nasreen et al. 2021: 1). A recent example of investment in key worker affordable rental housing is by Aware Super. It seeks to develop housing in New South Wales, Victoria and Western Australia to be rented at a 20 per cent discount on the market rent to key workers including teachers, nurses, emergency services and social workers (Aware Super n.d.).
- **Home modification grants:** Grants provided to support the costs of custom-built changes to homes, including rental housing, to make them more accessible and useable for people with disability. It covers both minor and complex home modifications, and is funded by the National Disability Insurance Agency (NDIA).

- **Social enterprise real estate agencies (SEREAs):** SEREAs are real estate companies that are generally owned and operated by not-for-profit organisations. SEREAs manage privately owned rental properties and invest the profits in new social and affordable housing. Prominent SEREAs include Homeground Real Estate and Urban Choices in Victoria; Elevate Residential and Purpose Real Estate in Queensland; and Key2Realty and Echo Realty in New South Wales.
- **HomeShare:** Elderly people or people in need of some form of assistance (who are generally homeowners) are matched with lodgers who provide a pre-agreed number of hours of support to the home provider in exchange for discounted or free rent. This mutually beneficial relationship is usually arranged and managed by SEREA organisations. Examples of prominent HomeShare organisations include AVIVO in Western Australia, Community Connections in ACT, Holdsworth Community in New South Wales, and Shared Lives Australia in Victoria.

3.2 Interviews

Twenty-nine interviews were conducted with small-scale landlords. Each interviewee was asked a range of questions about motivations, risk, impact of taxes and tax concessions, as well as market conditions, tenant selection, property damage, insurance, and residential tenancy legislation. The semi-structured interviews were conducted online using Microsoft Teams and the data were analysed using NVivo software.

3.2.1 Investment models

The interviews reveal two main business models (Table 5). The first model is positively geared *long-term hold investment* ([LTHI] Model 1) and the second is *short-term hold for capital gain investment* ([STHCGI] Model 2). While there was a tendency for the investors to adopt one or the other model, some used both. For example, an investor might draw down the equity in their first property (gained via Model 1) to purchase their subsequent property (Model 2) and in the process become negatively geared on both.

Across the sample, investors anticipated capital appreciation although it was not the primary motivation of many—and not all investors had actually made capital gains when they had sold properties. For example, Interviewee 20 sold at a loss due to poor initial research into the location. This reflects the investor naivety highlighted by Seelig, Thompson et al. (2009).

Many investors were concerned with building inter-generational equity to ensure their children had access to housing, which reflects a broad concern with declining housing affordability.

Access to an investment loan is a critical step in the investment journey. All interviewees stated that it had been simple and easy to obtain finance until recently. Those looking to refinance or purchase further property noted that credit had tightened significantly—and for some this meant further investment was out of reach or that refinancing had been difficult for them.

As the following sections indicate, many of these small-scale investors are struggling with increased interest rates—not simply for the investment property but because they are also servicing mortgages on their homes. This draws attention to role of prudential stress-testing requirements in the supply of private rental housing.

Table 5: Summary of investment model attributes

Feature	Model 1: LTHI	Model 2: STHCGI
Gearing strategy	Positive	Negative
Cashflow sensitivity	Highly sensitive	Insensitive
Income	Moderate income	High income
CGT discount	Non-critical	Critical
Loan type	Principal and interest loans	Interest-only loans
Affordable housing appetite	Moderate to high	Low
Asset management strategy	Self-managed, active	Inactive: avoid repair and maintenance through choice of property and tenant
Investment property type	Older, depreciated stock	Newer, minimum depreciation
Negative gearing	Used because of unanticipated losses	Intentional, enables higher leveraging

Source: Authors

Model 1: Long-term hold investors

Long-term hold investors (LTHI) are a mixture of:

- purposeful investors—many became property investors because family members (particularly parents) were small-scale investors
- accidental landlords—who inherited property or gained it because of a divorce.

LTHIs aim to supplement their other income through positively geared investment and seek to own their investment property outright by retirement, if not earlier. LTHIs prefer property to other forms of investment, as *'you cannot go wrong with property'* (Interviewee 10) and because it is *'safe and secure'* (Interviewees 15, 23). CGT is not a significant consideration, as most do not intend to sell their properties in the near future (Interviewees 2, 4, 12, 15, 24, 28). Some interviewees admitted that they *'don't know enough'* about how it works (Interviewee 2), which suggests a level of investor naivety (Seelig, Thompson et al. 2009). There was a widespread attitude that CGT was not a bad thing—profit is made, and it is fair to be required to pay tax on it.

LTHIs tended to have moderate incomes, and their wealth is comprised primarily of their own home and their investment property. The purposeful LTHIs acquired property as soon as they were able to afford an investment loan and service the other property-related costs. As the intention is to own the investment outright, they typically obtain a principal and interest loan. The combination of moderate income and the extent of leveraging means that these investors are highly sensitive to cashflow—particularly in the early years of the investment. Most had experienced increased expenses that reduced their investment profit, and many found themselves negatively geared, which they could ill-afford. (Negative gearing is when an investor offsets their losses against other income for tax purposes.) However, as some mentioned, only some of the loss is recouped through negative gearing, so they still experienced financial stress (Interviewees 2, 4, 6). Thus interest rate rises were causing anxiety.

LTHIs' attitudes to negative gearing varied little. To them, the aim of the investment is to make a profit rather than a loss, so it did not motivate their investment decision (Interviewees 6, 7, 12, 28). However, as negative gearing was available, they used it when their situation demanded it, and it was crucial in keeping them in the market (Interviewees 1, 3, 4, 5, 8, 10), especially at the early stages of the investment term (Interviewees 2, 3). Investors went further and stated that negative gearing is 'banged on as a big deal' but its practical benefit is limited (Interviewees 10, 12, 28). Given their cashflow-sensitivity, these investors were often faced with the need to increase rents—although they were generally reluctant to do so. Some LTHIs consider their position as landlords a *'fortunate position'* (Interviewee 10) and did not intend to take advantage of or impoverish their tenants for their own benefit, with some keeping their rents lower than market rent in consideration of their tenants' needs (Interviewees 10, 13, 11, 23, 26, 27). Others raised rent in keeping with interest rates and the general rental market due to their cashflow-sensitivity (Interviewees 13, 24).

Few LTHI landlords had active asset-management strategies, and instead undertook repairs and maintenance as required. One consequence of an LTH strategy is emotional connection to their properties and concern for its condition. This meant LTHIs were more ready to spend on maintenance than the STHCG investors. Many had the skills to undertake repairs themselves, which was a consideration when they purchased. It enabled them to buy less expensive, rundown properties that they could renovate cheaply.

Given their long-term strategy, LTHI landlords favoured buildings that were not too new because of their more limited borrowing capacity and their willingness to invest in maintenance or renovation, as necessary. They mostly chose properties in locations they were familiar with. For the multiple property owners, many concentrated their investment in a single locality that they had extensive knowledge about (e.g. Interviewee 27). Others invested interstate because they had been priced out of their own states (Interviewee 15). Tenant choice centred primarily on tenant ability to pay rent, and the perception they would care for the property (Interviewees 3,11, 26).

Some of these small-scale investors noted they were often portrayed by commentators and the media as *'extortionists'* (Interviewee 10) although they saw themselves as providing a basic human need (Interviewees 5, 6, 10). Interviewee 10 felt there was a need to distinguish between long-term landlords such as themselves and those who were flipping properties.

Short-Term Hold for Capital Gain Investors (STHCGI)

STHCGIs were a much smaller group than the LTH group (three out of 29). They tended to be higher-income and were less likely to be small-scale. They typically had portfolios of more than four properties, and/or held higher-value property as well as holding other types of assets. STHCGIs tended to be more sophisticated investors than the LTHIs, and were acutely aware of market trends, tax and other financial considerations.

As STHCGIs do not intend to hold the property long enough to pay off the mortgage, they tend to opt for interest-only loans instead of principal and interest loans, even though this attracts a higher interest rate. Their higher income allows them to absorb cost increases, and they are not especially cashflow-sensitive. Negative gearing is very important to them, as it reduces their personal income tax burden and enables higher leveraging. While offsetting rental losses does not fully cover the losses, they are compensated through capital gains. Thus, CGT is a prime consideration and the CGT concession is critical. Unlike the LTHIs, STHCGIs are not so sanguine about their capital gains being taxed and regarded it as exorbitant. The implication is that reducing the CGT concession amount would deter their investment:

> *Capital gains is in the back of my mind. The 50 per cent discount for owning it for more than 12 months is absolutely key. If there's going to be changes to that, then we'd have to have a look and see what's the best outcome for [future investments]. (Interviewee 22)*

The CGT concession is the key reason why STHCGIs hold their properties for at least 12 months—which is the minimum time required to qualify for the concession (Interviewees 3, 7, 22). The implication here is that STHCGIs are adept at identifying and obtaining properties that are undervalued, and would flip such properties immediately if there were no disincentive to do so. Without the CGT concession, these investors would likely be insignificant in the rental housing market.

STHCGIs buy newer properties that do not require renovation and have minimal maintenance requirements during the holding period. If maintenance is required, STHCGIs will only undertake it if it will lead to an increase in capital appreciation:

> *Do you think I should put things like, uh, improve the bathroom and the kitchen and things like that? … Not worth it. We're not going to make much extra rent for it. (Interviewee 3)*

Broader property strategy

A very small subset of investors use the tax benefits available to rental investors to pay off their home mortgages. They withdraw equity from their investment property to pay down their mortgage, as interest on the investment loan is tax deductable but interest on their home mortgage is not.

3.2.2 Land tax

Land tax was not a disincentive to investment where a requisite rate of return on investment could be achieved (Interviewee 25). However, increases in land tax post-purchase impact profitability (Interviewees 4, 5, 20, 23) and will prompt a rental increase if the market will bear it. However, many landlords, especially LTHIs, want to avoid increasing rents because of concern for the tenant (Interviewees 13, 20, 23) or the potential for tenant turnover, which is costly. The recent land tax increases in Victoria attracted criticism (Interviewees 4, 5, 20, 23). As land value forms the basis for land tax, it was argued that inner-city properties were no longer viable investments and thus increased land taxation would reduce the supply of private rental in these areas: '*In inner-city areas … a lot of people [are] not renting them out, because the land tax is so high*' (Interviewee 8).

3.2.3 Depreciation

Depreciation tax allowances were not seen as a consideration for the investors. Depreciation deductions are only useful for newer properties, and few of the small-scale investors had newer properties. This reflected decisions to purchase older properties because these were cheaper—a key metric for achieving their target rate of return on investment (Interviewees 1, 3, 23): *'The depreciation is just like such a small thing that I don't even consider it until tax time'* (Interviewee 23).

Additionally, the annual nature of the depreciation allowance reduces its impact for cashflow-sensitive LTHIs.

Those who did purchase newer investment properties, like Interviewee 13, claimed the depreciation allowance, but it was considered an insignificant factor. This in part arises as depreciation tax allowances form part of the calculation of CGT when a property is disposed of. Thus, for those who were motivated by capital gains, depreciation provided no financial benefit. Not all of the interviewees understood this when they purchased, and some were blindsided by this when they sold their property.

> *At the end of the day when you depreciate something … when you do your capital gains tax, what happens is that all the depreciations … are then clawed back by the government. (Interviewee 6)*

> *A lot of people don't understand … that it's added on at the end, that's when they get sold into that. (Interviewee 16)*

3.2.4 Interest rates and market conditions

Interest rate change was the key risk factor for most interviewees. It was seen as a determining factor before, during and after the decision to invest (Interviewees 2, 6, 7, 9). Increases in interest rates reduce investment profitability. For the STHCGI, their other income cushions the impact of interest increases. However, any LTHIs are significantly impacted by interest rate rises because of their cashflow sensitivity. And while interest is a tax deductable cost, the benefit only occurs at tax time—whereas interest is paid throughout the year.

Interest rate increases over and above expectations meant that some were considering selling their properties, or were holding off on buying additional investment properties (Interviewees 6, 2, 9).

> *It is going to be certainly difficult [to stay in the market] if the rate keeps rising. (Interviewee 4)*

> *The interest rates going up to where they are now … It's certainly causing us to have another look at it to see … if we're comfortable … to take the loss that we're receiving. (Interviewee 22)*

As discussed earlier, where landlords were able to, some passed interest rate costs on to tenants.

> *As interest rates have been increasing and the property has increased in value as well, we've been looking at keeping rents in line with that. (Interviewee 26)*

> *Rents keep on increasing [because] the landlords keep on passing the [interest] rates on. (Interviewee 18)*

Where possible, other landlords held off interest-rate-induced rent increases out of consideration for their tenants.

3.2.5 Tenant selection

Many interviewees identified tenants as a key investment risk, stating that a good tenant goes a long way to ensure the success of the investment property, while a bad tenant can derail the investment through:

- increased maintenance costs
- high tenant-turnover costs
- legal costs when tenancy disputes emerge.

Given their financial motivations, investors emphasised their preference for tenants with financial capacity and no propensity for property damage. All other considerations were secondary.

> *It doesn't really matter who's in there at the end of the day, does it? As long as they're happy to pay the rent on time and they take care of the property. (Interviewee 26)*

> *You are really looking to those key issues of paying the rent and property damage. (Interviewee 3)*

While most interviewees were indifferent about the tenant type beyond the two factors mentioned above, some also screened out smokers, pets and children (Interviewee 3).

Prior bad experiences with tenants prompted some investors to devise strategies to obtain 'good' tenants. This included personally interviewing prospective tenants and establishing good relationships with tenants to encourage better property care. The interviewees predominantly employed the services of real estate agents, with only a handful opting to manage the properties themselves. The tenant recruitment was primarily done by the agents, and the landlords mostly deferred to the agents' advice, as long as the conditions of financial capacity and property care were met. Those who managed their properties themselves were those who had property maintenance skills, had flexible jobs and lived in or near the neighbourhood, which enabled them to be directly involved with the management of the tenancy and property.

Many of the interviewees were concerned about rental affordability.

> *I'll make like a moral, ethical kind of … I'm mindful that, yes, I'm here to make money, and yes, these investments have to look after themselves. But I am also human. I also have a family. I value having an affordable roof over my head … I want to get the money as an investment return, I want to pay off the debt and whatever else, but I don't want to see the basic need of … housing as a human necessity become [something] for only the rich. (Interviewee 27)*

> *I worry about … the future generations of not just my children, but everyone else's children. And I actually don't like prices rising because it just ruins it for the whole … increases in price, the interest that people end up paying is continuing forever on a much larger principal and it just ruins it for everybody, especially when wages aren't increasing as much. (Interviewee 18)*

Many interviewees invested into lower-income areas and less valuable housing, as this was what they could afford and it provided a positively geared investment. In doing so, some recognised they were effectively catering to tenants eligible for social housing. However, some investors associated tenancy problems with low socio-economic cohorts. As Interviewee 27 argued:

> *I'm kind of done with the lower end of the market. They just seem to be … we have had a few that—I just probably caught in the wrong crowd. (Interviewee 27)*

Interviewee 2 suggested that investors be rewarded through tax and other financial concessions for taking in 'subprime' tenants.

3.2.6 Long-let vs short-let

Very few interviewees had given much thought to the short-let market. They largely perceived it as *'too much of a hassle'* (Interviewee 3). Short-lets require additional management—which they were aware was costly. Some landlords believed their property was not located in an area that would attract short-term letters. For others, the age or physical state of their property did not make it a desirable short-let property. For yet another group, the owner's corporation prohibited short-term letting.

However, one investor (Interviewee 1) had multiple apartment properties in an inner-city area that were listed on Airbnb. The investor managed the properties themself rather than contracting out, thus saving the considerable cost of property management. The investor obtained double the rental income compared to long-letting. This additional rental income enabled the properties to be positively geared despite extensive leveraging. This investor was aiming for a portfolio that could provide a passive income stream and enable early retirement. This investor also had a long-let property, with very long-term older tenants paying affordable rent in what is effectively a guaranteed life tenancy.

3.2.7 Knowledge of NRAS and social or affordable housing schemes

Those who invested in property for financial gain and not 'to solve social inequalities' (Interviewee 22) would only be interested in social or affordable housing schemes that allowed them to realise their requisite rate of return (Interviewees 12, 15, 20, 28). Most had heard of the NRAS scheme, but they knew nothing about it (Interviewees 23, 24, 25). This is not surprising, given the scheme closed around 10 years ago and the last rebates are ending. However, they were interested in the concept—with the proviso that any scheme needed to meet their financial goals.

As highlighted in section 4.2.5, some of the investors were providing affordable rents and housing people such as low-income earners they understood to be highly disadvantaged in the market (Interviewee 27), newly arrived students (Interviewee 17) and the elderly (Interviewee 1). CRA was regarded as important for low-income tenants, and most were willing to accept *'subprime'* tenants if assistance met the affordability gap.

3.2.8 Use of financial help

Seelig and Thompson et al. (2009) found that small-scale investors were unsophisticated and naïve. However, Pawson and Martin (2021) subsequently found increasing levels of professionalism. Our interviewees seldom consulted financial planners or property advisors before purchasing their property. Financial planners were seen to be too expensive (Interviewee 4). Only two interviewees had obtained professional advice with the verdict that were untrustworthy (Interviewee 8) and *'basically useless'* (Interviewee 27).

The investors in this study preferred to rely on the knowledge of friends and family, and to do their own research (Interviewees 1, 5, 27). Property podcasts, property websites and other social media channels were also popular sources of information.

3.2.9 Home sharing

Only one interviewee sublet rooms in their own home. Interviewee 17 let her spare room to students, tourists and other temporary lodgers for financial reasons, as well as for companionship. This had largely been a very positive experience and had mitigated the impact of several financial crises. She had declared this rental income to the ATO—but had been dismayed to subsequently learn that subletting would trigger CGT upon sale of the property.

3.2.10 Residential Tenancies Act

Most investors admitted they were largely unfamiliar with the Residential Tenancies Act (RTA). Their understanding of it related almost exclusively to their own experiences as former tenants, and from disputes with tenants. Property managers tended to handle RTA-related issues. However, the investors argued that in some states, tenancy legislation empowers tenants more than landlords, and increases their risk: *'Look, it is easy for the tenants to get away [with anything]'* (Interviewee 27).

Rental caps were criticised. The interviewees explained that where rent caps are enforced, their coping strategies were to either:

- increase the rent as significantly as possible to factor in the possible changes that might occur in the tenancy period
- sign shorter leases (6 months or less, if legal) to allow them to review their rents with each new tenant or lease.

3.2.11 Discussion

LTHI are a key source of affordable housing. Many LTH investors felt that the government *'does nothing'* to support their engagement with affordable housing (Interviewees 8, 12, 15, 20, 27). As they viewed it, they obtain a low rate of return on a large capital outlay, an outlay that involves significant monthly costs. They pay land tax, stamp duty and they or their beneficiaries pay CGT—but they receive no tax benefit if they are positively geared. While some understood that CRA helped tenants, it was not seen as assisting landlords.

STHCGI may not be a significant source of affordable housing, as they prefer higher-value properties. Interest-only loans mean that STCGI do not have the burden of principle repayment and their higher interest payments and land tax are mitigated by negative gearing. Multiple investments mean their liability for stamp duty and CGT is high. High income and wealth mean that stamp duty is not a significant barrier to investment. Most costs are capitalised at subsequent sale, so the CGT concession is a critical investment consideration.

These two models are the outcome of the financial capacities of the investors and reflect differing views of how wealth can be accumulated. The LTHI could be regarded as aspirational: some are successful, others less so. They accept a significant degree of risk over an extensive period to acquire property as a store of wealth.

LTHI sensitivity to cashflow is a major concern. It suggests that lending criteria may have been too liberal—and that many of these borrowers seemed to be exposed to risk they did not understand. Property investment websites and the like encourage these investors. This is consistent with Martin's (2018) work, which notes that Australian property investors often source information and advice from 'self-styled property investment mentors' and online property investor communities.

While STHCGIs may not be a key source of affordable rental properties, this investment strategy fuels house-price inflation, which impacts the capacity of LTHI (and aspiring homeowners) to enter the market. The frequent turnover of properties is a source of instability for tenants.

Housing price inflation appears to drive LTHI investment into lower-value localities and more highly depreciated stock, providing a source of affordable rental housing. It does not appear to drive the creation of new stock.

The cashflow sensitivity of LTHI meant there is considerable interest in affordable housing schemes if they provide investment security. However, while an NRAS-type scheme was of interest, it would need to address the monthly cashflow issue. Moreover, if such a scheme were intended to drive new supply, it would need to consider the price differentials between older, low-value stock and new housing. LTHI have modest incomes that limit the amount of equity they can put into an investment, and the investment must 'carry itself'.

For home-sharers, the treatment of their properties (at least partially) as investment properties and the accompanying effect of CGT serves as a disincentive. This means that under-used homes that could serve as a form of transitional affordable housing for low-income households are withheld from the market—which exerts further pressure on the existing supply. As noted in Faulkner, Sharam et al. (2023), home-sharing constitutes a potentially significant source of affordable housing.

3.3 Policy development implications

Investors engage in the property market for one primary reason: financial gain.

LTHIs provide stable, ongoing rental housing. They invest in varied locations and markets, and many provide housing for low- to moderate-income households. However, many LTHIs assume risk they are not capable of carrying. The most significant risk relates to cashflow. STHCGIs can carry the risk but are a source of unstable tenancies and, as speculators, contribute to housing price inflation.

These two types of investors reflect two business models: rental housing provision (being a cashflow business) or speculative trading of property. The three main government measures affecting investment are negative gearing, land tax and CGT concessions. Negative gearing does not address cashflow risk, although it does improve the annual rate of return. This means that negative gearing has reduced utility for LTHIs but encourages STHCGIs. Land tax is an annual cost that reduces the rate of return. It is a short-term holding cost for STHCGI but is more significant for LTHIs—particularly if the rate changes. CGT concessions incentivise STHCGIs, but not LTHIs.

LTHIs present a dilemma for policy makers. They provide the backbone of affordable rental housing, but some proportion of them should probably not be in the market. Given the centrality of leveraging, prudential requirements could be used to filter out more vulnerable investors.

LTHIs need incentives that address their cashflow needs. These could include:

- NRAS-like schemes targeting new supply that, rather than providing an annual tax concession, include monthly support payments.
- Increasing CRA, because this enables landlords to capture higher rents.
- Private rental headlease schemes offering incentives such as payment guarantees and make-good provisions for property damage.

To deter STCGIs, and to moderate house-price inflation, CGT concessions should be reduced and the holding period requirements extended.

LTHI incentives could be funded by reducing the participation of STHCGIs in the market (STHCGIs routinely make use of negative gearing and CGT concessions).

4. Findings from the discrete choice experiment survey

- **According to our survey, the average small-scale investor would need a tax offset or equivalent of roughly $650 per year for every 1 per cent of market discount provided.**
- **We found that investors are 12 per cent more likely to participate in schemes that provide a rental guarantee. They also prefer schemes that do not 'lock in' their property for an extended time period.**
- **The average investor in our sample would be willing to give up about $7,150 in annual tax rebates if there was a 'make-good' provision. Similarly, they are 7 per cent more likely to participate in schemes offering 'make-good' conditions.**
- **Between 40 and 60 per cent of investors would be willing to participate in schemes similar to NRAS or headleasing.**

4.1 Discrete choice experiment survey

This chapter reports findings from an online discrete choice experiment (DCE) survey of 800 small-scale property investors conducted over September–October 2023. Section 5.2 describes the survey instrument. Section 5.3 undertakes a descriptive analysis of the investors and their portfolio of investment properties. Section 5.4 presents findings from our analysis of the DCE data—particularly investor preferences for offering their investment property for rental through affordable rental housing schemes.

4.2 Survey design

The objectives of the survey were to understand the impacts of regulations, taxes, and other policy levers on small-scale investor preferences for participation in affordable rental housing schemes. We are particularly interested in the following:

1. Quantifying the marginal effects of different scheme-specific attributes on investor participation
2. Identifying the relative importance of each attribute; and
3. Predicting investor participation rates for different future schemes—including those that vary substantially from historic schemes trialled previously.

The online survey instrument was designed following a three-stage process. First, based on our literature review, we formulated a first draft of the instrument. Second, the research team undertook multiple rounds of testing the survey instrument, where we amended the instrument to reflect any issues or concerns that arose during testing. Third, the survey instrument was piloted with a sample of 50 respondents. Following analysis of this data, the survey instrument was revised a final time.

The final instrument comprised six broad sections:

1. **Screening questions:** The survey began with a set of screening questions to ensure respondents were eligible to take the survey, based on our definition of the sampling frame. In particular, study participants had to be at least 18 years old and own at least one investment property.
2. **Current place of residence:** This section was designed to understand the respondent's current place of residence, both in terms of the house dwelling itself (e.g. house type, number of bedrooms, location), as well as details pertaining relating to their tenure arrangement (e.g. monthly rent or mortgage repayments, lease period).
3. **Investment property portfolio:** Respondents were asked to indicate the number of investment properties that they currently own; subsequent questions requested further details about up to three investment properties in their portfolio. Among other variables, we sought details: location, year of purchase, type of housing, financing, tenancy, and participation in affordable rental housing schemes.
4. **Discrete choice experiments (DCEs):** This section presented respondents with eight discrete choice experiments each, such as the one shown in Figure 1, where they were presented with the choice of offering one of their investment properties for rental through one of two competing affordable rental housing schemes. The two schemes were defined in terms of multiple attributes, such as scheme duration, tenant eligibility, tax incentives and other conditions, as shown in Figure 1. For each scenario, respondents were asked to select their preferred affordable rental housing scheme, and whether or not they would participate in their preferred scheme if it were actually available on the market. Alternative attributes were systematically manipulated across respondents and scenarios in a bid to understand how different investors value each of these attributes differently, across the range of values shown in Table 6, to maximise statistical efficiency.
5. **Attitudes and perceptions:** Respondents were asked about their opinions on the current state of the housing rental market, the role of government in providing affordable rental housing, and their own attitudes towards participating in affordable rental housing schemes.
6. **Socio-demographic characteristics:** The final section of the survey collected information on respondents' socio-demographic characteristics.

The survey concluded with an open text question to elicit any feedback from respondents about the survey itself. Respondent feedback was largely positive, and specific comments indicated a high level of engagement and interest in the topic:

> *'[Affordable rental housing schemes are a] great idea for investors and investment properties.' (Respondent ID 3800)*
>
> *'Very interesting topic and useful insight.' (Respondent ID 595)*
>
> *'I found this survey interesting. I didn't know about all the different types of rental arrangements.' (Respondent ID 4132)*

Respondents also used the feedback section to note their understanding of and concern for the complex needs of renters and of landlords:

> *'it is very difficult for young people to get a foot in the door of owning a home today.' (Respondent ID 873)*

> *'I hope the government will prove financial support for low -income renters and affordable interest rates for landlords.' (Respondent ID 629)*

> *'Why is [the low rental vacancy rate] investors' problem? Some people like me use the rent from the property to survive—not all landlords are rich property moguls. Some people like to be self-reliant and not use government benefits.' (Respondent ID 784)*

> *'The government is making it harder on investors, so there will be a number of them [investors] that will now sell and reduce the number of properties available to rent in the marketplace.' (Respondent ID 881)*

> *'My main income is rental, since retirement. If the rental income cannot beat the current cost-of-living pressures and mortgage payments, [then] there is no point hanging on to the rentals anymore. I'm not entitled to social security assistance due to the ownership of two rentals. In reality, those two properties do not generate sufficient annual income to cover the overheads. What is the point of being a property owner?' (Respondent ID 3088)*

While one respondent noted their anger with support for recipients of schemes:

> *'It is too easy for [some people] to get housing and abuse the privilege.' (Respondent ID 2348)*

Figure 1: Example discrete choice experiment to elicit investor preferences for different affordable rental housing schemes

Scenario 1 of 8

We would like you to consider your investment property, a flat or apartment in a nine or more-storey block located in 2000, Sydney, NSW, which was purchased in 2015.

Imagine that you have the chance to participate your above investment property in the following affordable rental housing schemes. Assume that the schemes are comparable in all other regards. Which scheme would you prefer to participate in?

Hover your cursor over the blue text for more information.

	Scheme A	Scheme B
Scheme conditions		
Scheme duration	15 years	9 years
Condition on rental charges	Rent needs to be at least 15% below market rate	Rent needs to be at least 20% below market rate
Tenancy eligibility	Tenants must be in the lowest 75% income bracket	Tenants must be in the lowest 40% income bracket
Tax offset/payment to you	$35,000 per year	$9,500 per year
Tenant Acquisition Responsibility	Scheme provider	Landlord/owner or their agent
Penalty in breaking the scheme (early exit fee)	4% of the current incentive payment multipled by the number of years left in the 15 year term	6% of the current incentive payment multipled by the number of years left in the 9 year term
Rental guarantee	Yes	No
Make good condition	Yes	No
Option to continue the scheme	No	Yes
Maximum vacancy period for the property to be eligible	16 weeks	4 weeks
Preferred scheme:	○	○

Source: Authors

Table 6: List of DCE attributes and their values across different scenarios

Attribute	Definition	Potential values	
Scheme duration	Refers to the specified length of time or period during which the program or initiative is designed to operate.	1 year	12 years
		3 years	15 years
		6 years	18 years
		9 years	21 years
Condition on rental charges	Refers to a stipulation or requirement regarding the percentage at which the property can be rented in relation to the below-market rates. In other words, it outlines the condition or restriction on the amount a property owner or landlord can charge for rent, specifying that it should be a certain percentage below the prevailing market rates.	10%	20%
		15%	25%
Tenancy eligibility	Refers to the criteria or conditions that determine a tenant's qualification based on their income.	40%	60%
		45%	65%
		50%	70%
		55%	75%
Tax offset / payment to you	Refers to a financial benefit provided to property owners or investors as an incentive for participating in such schemes. This benefit in this survey is in the form of a reduction in the amount of tax owed or a direct payment to the property owner.	$9,500	$26,500
		$18,000	$35,000
Tenant acquisition responsibility	Refers to the obligations and tasks associated with acquiring tenants for a property.	Landlord / owner or their agent	Scheme provider
Penalty in breaking the scheme (early exit fee)	Refers to a financial consequence or fee imposed on a participant or investor who decides to exit the scheme before the agreed-upon duration or term, expressed as a percentage of the tax offset multiplied by the number of years left in the scheme	No penalty	6%
		2%	8%
		4%	10%
Rental guarantee	Refers to a commitment or assurance provided by the scheme provider that guarantees a specific level of rental income for a designated period.	Yes	No
Make-good condition	Refers to the requirement for scheme provider to return the rented property to a specified condition at the end of the lease or occupancy period.	Yes	No
Option to continue the scheme	Refers to the opportunity or provision for extending or renewing the participation in the specific housing program.	Yes	No
Maximum vacancy period for the property to be eligible	Refers to the allowable duration during which a property can remain unoccupied without losing its eligibility for participation in the scheme.	4 weeks	12 weeks
		8 weeks	16 weeks

Source: Authors

4.3 Sample description

Our sample comprised 800 small-scale Australian property investors. Survey participants were recruited through two market research companies: Pureprofile and TGM Research. We compared our sample to the target population, based on the same ATO statistics reported in Section 2.3 when characterising the demographic profile of small-scale property investors in Australia. As shown in Table 7, roughly 98 per cent of investors in our sample have fewer than five investment properties, and almost 80 per cent (79.6%) of our sample have one investment property. These percentages confirm the small-scale nature of the respondents' investment portfolios, and the sample distribution is broadly consistent with the target population.

However, as shown in Table 8 and Table 9, compared to the average Australian small-scale property investor, our sample tends to be younger and have higher incomes. For example, 23 per cent of our sample were under 30 years of age, while only 4 per cent of the target population are under 30. And 45 per cent of our sample were in the highest wage brackets (over $100,001) while only 29 per cent of the target group were in the highest wage brackets.

Table 7: Sample and target distribution in terms of number of properties owned

Number of rental properties	Sample		Target*
	n	%	%
1 rental property	637	79.6%	71.5
2 rental properties	109	13.6%	18.8
3 rental properties	34	4.3%	5.8
4 rental properties	9	1.1%	2.1
5 rental properties	2	0.3%	0.9
6 or more rental properties	9	1.1%	0.9

* Source: ATO taxation statistics (2019–20)

Table 8: Sample and target distribution in terms of age of property owner

Age range	Sample		Target*	
	n	%	n	%
Less than 30	266	23.2%	96,704	4.3
30–39	403	35.1%	455,227	20.4
40–49	246	21.4%	550,462	24.7
50–59	109	9.5%	571,927	25.7
60 or more	124	10.8%	552,521	24.8

* Source: ATO taxation statistics (2019–20)

Table 9: Sample and target distribution in terms of income of property owner

<table>
<tr><th>Taxable income group</th><th colspan="2">Sample</th><th>Target*</th></tr>
<tr><th></th><th>n</th><th>%</th><th>%</th></tr>
<tr><td>Less than $18,200</td><td>87</td><td>7.6%</td><td>14.5%</td></tr>
<tr><td>$18,200–$50,000</td><td>165</td><td>14.4%</td><td>23.5%</td></tr>
<tr><td>$50,001–$100,000</td><td>385</td><td>33.5%</td><td>32.6%</td></tr>
<tr><td>$100,001–$500,000</td><td rowspan="2">511</td><td rowspan="2">44.5%</td><td>28.4%</td></tr>
<tr><td>More than $500,000</td><td>1.0%</td></tr>
</table>

* Source: ATO taxation statistics (2019–20)

In terms of geography, as shown in Table 10, we have a good spread of investors in our sample across all states and territories, and a sufficient number of investors located in both major metropolitan areas and regional areas. As shown in Table 11, the majority of investors (73.6%) prefer to invest in properties located in the same metropolitan or regional areas as their place of residence.

Table 10: Sample distribution in terms of current place of residence

Greater Sydney	192
Rest of NSW	61
Greater Melbourne	209
Rest of Victoria	37
Greater Brisbane	79
Rest of Queensland	58
Greater Adelaide	65
Rest of SA	12
Greater Perth	54
Rest of WA	5
Greater Hobart	10
Rest of Tasmania	6
Northern Territory	1
Australian Capital Territory	11

Source: Authors

Table 11: Location of investment property, conditional on location of place of residence

	Invest in the same metropolitan area as they live	Invest in the metropolitan area in a different state	Invest in regional area in same state	Invest in regional area in a different state	Total
Live in metro	72.4%	2.9%	2.1%	0.9%	78.2%
Live in regional	1.2%	0.5%	19.4%	0.7%	21.8%

Source: Authors

Table 12 lists the relative importance of different investment strategies for investors in our sample. We found that the majority (45.8%) of small-scale property investors are highly sensitive to cashflows, and positive cashflows are the most important consideration when selecting an investment property. A significant proportion of investors also prioritise long-term capital gains (26.5%), stability (18.7%) and portfolio diversification (11.2%). The proportion of investors that invest with either a view to 'flip' the property (3.7%), or to generate income through short-term rentals (2.6%), is very small, indicating that these objectives only hold appeal to niche submarkets.

Table 13 summarises investor attitudes to different investment strategies, based on responses to different Likert-scale questions. In general, responses are consistent with Table 12. The majority of investors in our sample want to own their investment property outright before they retire (68%); they expect the value of their property to appreciate faster than interest rates (65.7%); and they expect their property to generate positive cashflows immediately (63.5%). Conversely, the majority of investors were not interested in the short-term rental market (60.9%).

Table 12: Ranked importance of different investment strategies, small-scale investors

Investment strategy	Mean ranking	Proportion of investors that ranked strategy as most important
Cashflow: Property should generate consistent rental income and positive cashflow.	2.36	45.8%
Capital gain: Property should have capital appreciation greater than interest rate on my mortgage.	2.70	26.5%
Long-term stability: Seeking properties for long-term wealth building and stability.	2.99	18.7%
Portfolio diversification: Risk diversifying your investments by acquiring various types of properties or in different locations.	3.47	11.2%
Fix and flip: Purchasing properties with the intention of renovating and selling them quickly for a profit.	4.38	3.7%
Vacation rentals: Investing in properties specifically for short-term vacation rentals.	5.10	2.6%

Source: Authors

Note: Results based on responses from the 800 small-scale investors who participated in our quantitative nationwide survey.

Table 13: Attitudes towards different investment strategies

Measure	Mean rating	Distribution				
		1 - Strongly disagree	2 -Somewhat disagree	3 - Neither agree or disagree	4 - Somewhat agree	5 - Strongly agree
My aim is to own my investment property outright by retirement at the latest.	3.9	1.6%	6.2%	24.1%	38.9%	29.1%
My investment property should have capital growth greater than the interest rate on my mortgage.	3.8	2.5%	6.9%	24.9%	38.2%	27.5%
My investment property should generate an immediate positive cashflow.	3.7	2.9%	7.9%	25.8%	42.5%	21.0%
My investment property will enable me pay off the mortgage on my primary place residence faster.	3.7	4.1%	7.5%	24.6%	40.6%	23.1%
I am not interested in the short-let rental market (e.g. Airbnb).	3.7	4.6%	11.6%	22.9%	33.0%	27.9%
I prefer high value high rental income to lower value lower rental income properties.	3.7	2.2%	8.0%	30.9%	38.1%	20.8%
My investment strategy includes acquiring various types of properties in different locations.	3.4	6.2%	12.0%	31.0%	34.2%	16.5%
My investment strategy is to hold property for short periods, negatively gear and realise profit through capital gains.	3.4	6.4%	14.8%	26.8%	34.9%	17.2%

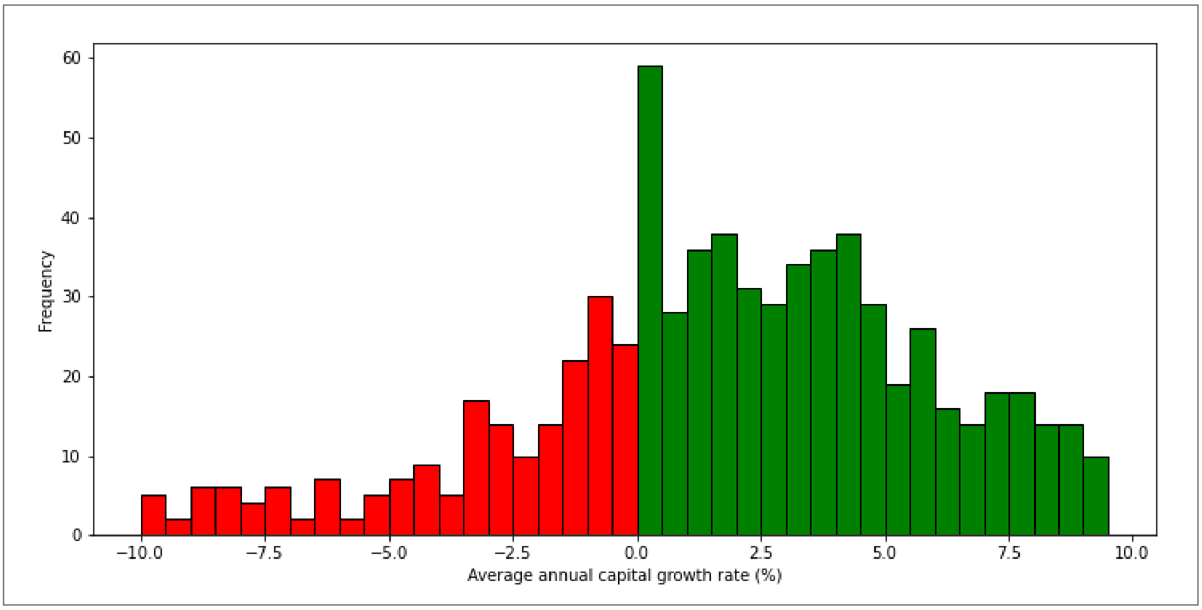
Source: Authors

In the following paragraphs, we examine responses to other survey questions that can shed further insight on the motivators behind these different investment strategies, and what they might imply for investor participation in affordable rental housing schemes.

In terms of financing, 58 per cent of the investment properties in our sample were purchased outright. Of the remaining 42 per cent of properties that were purchased with a mortgage, the mortgage has been paid off for 30 per cent of these properties. Roughly 29 per cent of the investment properties in our sample still have mortgage payments, and cashflow might be an issue for this subset of investors.

In terms of capital gains, the average investment property in our sample has appreciated on average by 5.3 per cent per year. But there is considerable heterogeneity in our sample, as can be seen from Figure 2. Roughly 26 per cent of the investment properties in our sample have depreciated in value.

Figure 2: Average annual capital growth rates across investment properties in our sample



Source: Authors

In terms of use, 72 per cent of the investment properties in our sample are currently being rented out. Of these, 90 per cent are being rented with long lease periods of six months or more, while the remainder are being rented with shorter leases. This corroborates our earlier finding that income from short-term rentals as an investment strategy is only preferred by a small proportion of investors. As shown in Table 14, of the 287 properties that are not currently being rented, roughly a third (30%) are being held for personal use, while the remainder are either being renovated (37%), for sale (11%), or on the rental market (19%).

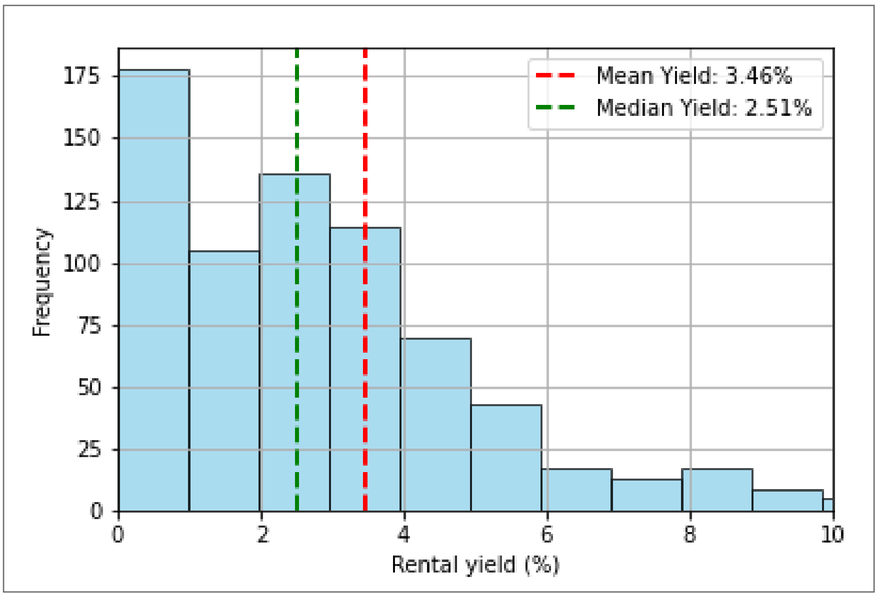
Table 14: 'Why is your investment property not currently rented out?'

Response	Count	Percentage
Undergoing renovations or maintenance work	107	37%
Currently seeking a new tenant	55	19%
Property is currently for sale	32	11%
Personal use (e.g. vacation home)	85	30%
Other (please specify)	8	3%
Total	287	100%

Source: Authors

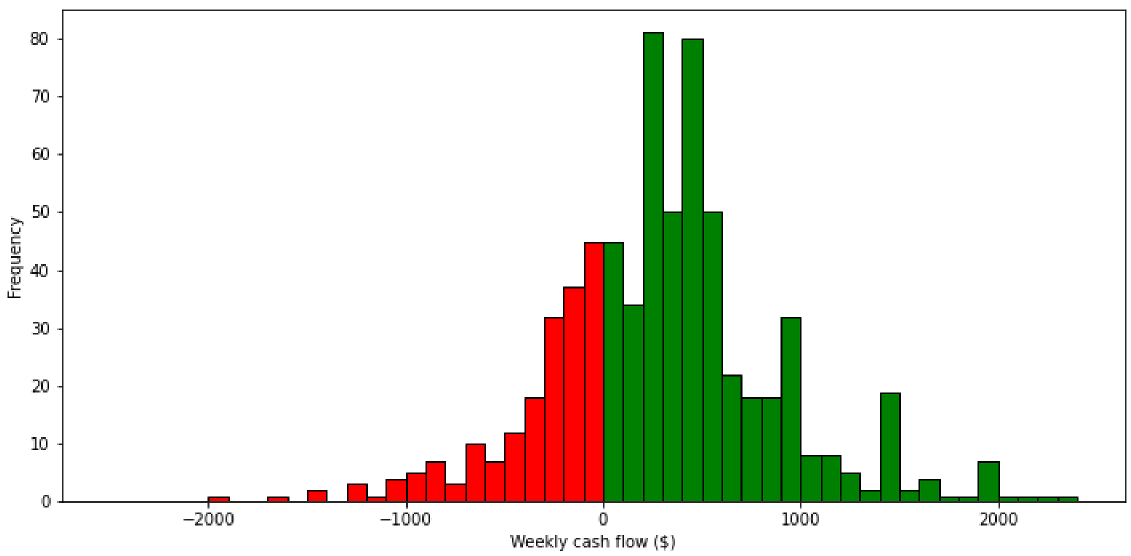
Rental yields for investment properties in our sample that are currently being rented out are on the lower side, as shown in Figure 3. The mean and median rental yields are 3.5 and 2.5 per cent, respectively, where rental yields have been calculated as the ratio of current annual rent to current market value, assuming that the vacancy rate is zero. Figure 4 plots the distribution of weekly cashflows for these properties, defined as the difference between rents on one hand, and mortgage payments and operating costs on the other. Roughly 26 per cent of these properties are generating negative cashflows, but the remainder have positive cashflows, which indicates that low rental yields are still profitable for the majority of investors in our sample. This is consistent with respondents' self-reported measures of satisfaction with their investment property.

Figure 3: Distribution of rental yields across investment properties in our sample



Source: Authors

Figure 4: Cashflows across investment properties in our sample that are currently being rented out



Source: Authors

In terms of current participation in affordable rental housing schemes, roughly 24 per cent of investors in our sample are currently renting at least one investment property through the National Rental Affordability Scheme (NRAS), 15 per cent are renting through headleasing, and 7 per cent are renting though Defence Housing. Due to the small sample size of Defence Housing investors, we do not separate these out in our analysis below.

As shown in Table 15, the majority of investors in our sample are satisfied with the rent that they are receiving (74%), and the net return on their investment property (71.6%). While sample sizes are smaller for some of these subgroups, and any figures should be interpreted with caution, our findings indicate that investors who are participating in the NRAS are more likely to report they are very satisfied (50.5%) with the performance of their investment property than the average investor in our sample (35.3%). Conversely, investors who are participating in headleasing schemes appear to be slightly more dissatisfied with the overall scheme (13.2%) than the average investor (4.6%).

Table 15: Level of satisfaction with investment property

Measure	N	Response				
		Very dissatisfied	Somewhat dissatisfied	Neither satisfied nor dissatisfied	Somewhat satisfied	Very satisfied
I am satisfied with the rent I am receiving						
All	730	4.0%	7.9%	14.1%	43.3%	30.7%
NRAS	99	2.0%	5.1%	9.1%	45.5%	38.4%
Headleasing	38	2.6%	10.5%	18.4%	47.4%	21.1%
I am satisfied with the return on investment						
All	730	4.1%	8.4%	15.9%	36.3%	35.3%
NRAS	99	1.0%	4.0%	11.1%	33.3%	50.5%
Headleasing	38	5.3%	13.2%	13.2%	50.0%	18.4%
I am satisfied with the tenant living in the property						
All	730	2.2%	4.7%	16.2%	37.5%	39.5%
NRAS	99	1.0%	1.0%	18.2%	34.3%	45.5%
Headleasing	38	2.6%	5.3%	18.4%	39.5%	34.2%
I am satisfied with the social housing scheme for my investment property						
All	306	1.0%	3.6%	14.1%	37.3%	44.1%
NRAS	99	0.0%	3.0%	11.1%	36.4%	49.5%
Headleasing	38	5.3%	7.9%	15.8%	52.6%	18.4%

Source: Authors

4.3.1 Policy development implications: Investor preferences for participation in affordable rental housing schemes

Responses to the DCEs were used to estimate a multinomial logit model of investor preferences for participation in affordable rental housing schemes. Each of our 800 survey respondents was presented with eight distinct DCEs (shown in Figure 1), where they were given the choice to offer one of their investment properties for rental through one of two competing affordable rental housing schemes. The two schemes were defined in terms of multiple attributes, such as scheme duration, tenant eligibility, tax incentives and other conditions.

The multinomial logit model was used to model the choice between these two competing schemes across different scenarios and respondents, and the utility of each scheme was specified to be linear in the scheme-specific attributes. It is important to note that our sample differs from the target population in terms of age and income, which are exogenous, and the multinomial logit model implicitly controls for differences in exogenous variables between the sample and the target population. Estimation results are reported in Table 16. Our findings may be summarised in terms of four key points.

1. Financial conditions

The financial conditions of the scheme are the most important determinant of investor participation—which further confirms the importance of positive cashflows to the majority of investors. Based on our model results, we are able to establish the level of subsidy investors would require in exchange for providing a rental discount. The average small-scale investor would need a tax offset (or equivalent) of roughly $650 per year for every 1 per cent market discount provided. They also indicated they strongly value schemes that assure rental income over a specific period. All else being equal, investors are 12 per cent more likely to participate in a scheme that provides a rental guarantee.

2. Flexibility

Investors value flexibility over stability. All else being equal, investors prefer schemes that have shorter durations that do not lock in their property for an extended period of time. However, the impact of other related scheme attributes—such as penalties for early exit and the opportunity for rollover—were not found to be statistically significant, which suggests that these attributes are not as important.

3. Make-good provisions

Conditions relating to tenancy are very important. Investors have a strong preference for schemes that offer make-good conditions—that is, schemes that require the scheme provider to return the property to the original condition at the end of the lease. The average investor in our sample would be willing to give up roughly $7,150 in annual tax rebates if there was a make-good provision. Alternatively, all else being equal, the average investor in our sample is 7 per cent more likely to participate in a scheme that offers make-good conditions rather than one that does not. Relatedly, investors prefer schemes that allow them to lease to higher-income households. Our model allows us to put a price on what it would take for them to accept lower-income households. A penalty of roughly $240 applies for accepting tenants from a 1 percentile lower income bracket. In other words, all else being equal, the average investor would require at least $2,400 in annual tax rebates to house tenants in an income bracket that is 10 per cent lower.

4. Investor participation

We use our model to predict investor participation in different types of affordable rental housing schemes. In general, we find that between 40 and 60 per cent of investors in our sample would be willing to participate in schemes similar to NRAS or headleasing, in terms of the variables included in our model and described earlier. This is significantly higher than expected, given the participation rates in existing schemes. This suggests that many investors are not aware of the existence of these schemes and the incentives they offer. From a policy perspective, there is a need to develop a more effective communication strategy to incentivise investor participation.

Table 16: Estimation results from multinomial logit model of investor preferences for participation in affordable rental housing schemes

Variable	Estimate	P-value	Odds ratio	Compensating annual tax differential
Scheme attribute				
Financial conditions				
Condition (i.e. discount) on rental charges (% below market rate)	-0.643	0.00	0.94	$643
Rental guarantee	0.095	0.00	1.10	$9,530
Tax offset/payment to you	0.100	0.00		-
Stability and flexibility				
Scheme duration (years)	-0.014	0.00	0.99	-
Option to continue the scheme	0.000	-	1.00	-
Penalty in breaking the scheme (early exit fee) (% of tax rebate)	0.000	-	1.00	-
Tenancy conditions				
Make-good conditions	0.072	0.00	1.07	$7,150
Tenancy eligibility (income per centile)	-0.243	0.02	0.78	$243
Tenant acquisition				
Maximum vacancy period for the property to be eligible (weeks)	0.000	-	1.00	-
Tenant acquisition responsibility rests with landlord	0.030	0.19	1.03	$3,020
Non-participation				
Utility of not participating in any affordable rental housing scheme	-0.526	0.00	0.59	-

Source: Authors

5. Policy workshop: navigating the ‘difficult middle ground’ to stable small-scale investment

- **Education may assist some small-scale investors to make better investment decisions.**
- **Investors exiting the National Rental Affordability Scheme has resulted in the loss of affordable housing, placing significant pressure on some housing markets.**
- **Headleasing provides benefits to investors and tenants. It is the preferred way to capture private stock.**
- **Savvy private investors who benefit from tax concessions increase stock availability. However, there are opportunities to adjust tax incentives and achieve better community housing outcomes.**
- **Policy makers prefer to support CHPs to build long-term solutions through capital investment. However, it was recognised that a for-profit small-scale investor has a role to play in ensuring stock levels can meet demand.**

5.1 Policy workshop

Nine policy makers at director or executive director level from federal and state treasuries, the Department of Social Services, and state and territory housing programs participated in a workshop to discuss key issues identified through the quantitative survey and other qualitative work undertaken earlier in the research program. These key issues were:

- the impact of cashflow on investment decisions and returns
- the effectiveness of various incentive schemes
- the impact of tax incentives on investment decisions.

Final reflections were canvassed so that each participant had the opportunity to synthesise their ideas based on the full discussion of all topics.

5.2 Cashflow considerations: rental vacancies and interest rate rises

The research revealed that cashflow was an important consideration for long-term hold investors (LTHIs) who have a modest income and seek to be positively geared from the outset of their investment. When unexpected changes caused financial hardship for these investors, it was difficult for them to hold on to their properties. When LTHIs opt out of their real estate investment, it creates instability for their often-vulnerable tenants.

Two areas of concern were discussed in relation to financial hardship for these small-scale investors:

- variations in rental income
- interest rate rises.

Unintentional losses through variations in rental income could be mitigated by programs such as headleasing schemes run through collaboration with CHPs. In this model, investors receive a guarantee of a regular, stipulated rental income, and assurance that their property will be returned to them in good condition at the end of the lease. This was seen to incentivise this group of investors, and ease their cashflow concerns:

> *The certainty of a rental return and the lease terms where government or CHP has to return the property at the same level, like ‘make-good’, and return it back, that can be quite attractive. So, they can actually rent the property out long-term to the government or to a CHP, and the government or CHP is the renter, not the actual vulnerable tenant. (Participant 1)*

However, schemes such as these might not be enough for some investors to withstand financial hardships associated with interest rate rises. Interest rate rises were identified as the most significant concern in relation to cashflow, as they create direct month-to-month budget problems for these LTHIs. Sometimes investors experienced financial hardship due to interest rate rises during their headlease timeframe. However, their rental tenancy agreement meant that they were committed to maintain the rental price for the term of the lease, despite their financial hardship. At the end of the 10-year period, these investors were unlikely to extend the option on the lease:

> *There’s been a couple [of investors] that have said that they want to sell out of it because of financial hardship, but that’s been probably 1 per cent of the portfolio. (Participant 3)*

While this is a small proportion of investors, the negative consequences of this effect were substantial. It resulted in the investor experiencing financial hardship, which led to them selling the property, and the tenant then experiencing instability associated with the sale of the property, which often led to increases in rent. Participant 1 noted that indexing rent on headleases to allow them to keep up with real rent prices was an important mechanism to address this concern.

Workshop participants noted that while small-scale investors were important in the community housing ecosystem, they would prefer to work with large-scale investors, who presented a smaller risk. Small-scale investors generated instability in the market because they were highly vulnerable to interest rate changes; when interest rates rose, they were the group most likely to experience financial hardship and be forced to sell, creating disruption for tenants.

> *If we do have these small-scale investors who are not necessarily financially savvy, or aren’t necessarily making high returns, I do wonder if there’s a risk in depending on them to provide affordable housing. (Participant 5)*

Education was proposed as one way to mitigate this risk:

> *I do think that educating these types of investors into just thinking about where interest rates might go in the future before they make their investment is just a sensible thing. (Participant 4)*

5.3 NRAS and headleasing: risks and benefits of incentive schemes

During this part of the workshop, participants discussed the NRAS and continued to discuss headleasing. The associated costs and benefits of the schemes were considered, especially in relation to unintended outcomes at the expiration of NRAS and costs associated with make-good provisions on headleases.

5.3.1 NRAS

The ending of NRAS subsidies has resulted in the loss of affordable housing stock through two mechanisms. Firstly, investors were likely to increase rental prices at the end of the 10-year NRAS scheme: *'Most of those owners will choose to put their rents up'* (Participant 2).

Secondly, it was noted that once NRAS incentive schemes ceased, investors were likely to sell their properties, creating increased instability for tenants. In Queensland, a large proportion of privately owned stock is being returned to the general rental market or sold. The scale of disruption to tenants who face a very low vacancy rate and high rents has prompted the Queensland government to purchase some of this stock.

> *The people in those properties can't afford [increased rents], and so that's why the government has had to step in and actually purchase those properties where that's possible. (Participant 2)*

Placing these properties into the ownership of CHPs has the benefit of longer-term stability, and it was noted that obtaining those properties *'in perpetuity would be a major policy outcome'* (Participant 8).

Overall, the outcome from the NRAS discussion was that CHPs were better able to provide long-term stock availability and tenancy stability than private investors.

5.4 Headleasing

Headleasing was identified a preferred way of capturing private stock. Headleasing provides flexibility and ongoing stability and security for both parties. Headleasing is used to:

- counter short lets
- provide social housing
- ensure key workers have access to housing in appropriate locations.

The headleasing model was found to be very successful and popular with investors because it provided certainty with regard to their cashflow, and reliable professional tenancy management services. Tenants also benefitted from the stability provided by ongoing ownership. Programs should be no longer than 15 years to avoid the increased costs of maintenance as the asset ages. Participant 3 noted that 16 per cent of the rent was required to fund maintenance and the make-good provision.

5.4.1 Short-stay accommodation and headleasing

In Tasmania, where short-stay accommodation was having a significant impact on housing availability, a headleasing program had significant success in drawing investors out of the short-stay accommodation market and into the affordable housing market. In this program, investors responded to both the financial and social incentives on offer: '*They actually want to do something for the community. They want to help people who are on the housing register'* (Participant 9).

While the 'heart' was an important part of the success of the program, the financial incentives were also significant. The Tasmanian government paid:

- the rental gap so that the investors received above-market rent
- fees to the CHP to manage the tenancy
- a financial buffer to cover any property damage.

These costs made the program relatively expensive. However, it was seen to provide good value for money—especially in the context of low levels of affordable rental housing.

While investors on this program received less than short-stay market rent, they were satisfied with the guaranteed above-market rent, the professional management of the property, the strict screening processes, and the two-year rent guarantee they received. The program was so successful that there was a glut of investors wanting to take part, and an investor waitlist had to be created.

> *There's always a constant list of people wanting to be part of the program and we actually say, 'No, we've got no more money.' (Participant 9)*

5.4.2 Tenants are the greatest risk to investment

Tenants housed under headleasing schemes were considered to be the biggest investment risk because of the potential for property damage. Broadly speaking, affordable housing tenants were viewed to be lower risk, as they were in the workforce and therefore not spending as much time in their homes. These tenants may be key workers who have difficulty accessing housing due to extremely tight market conditions in their jurisdiction. On the other hand, social housing tenants were viewed as higher risk for property damage because their houses experienced more wear and tear, as they were out of the workforce and therefore home more often. It was agreed that on average, it would require approximately $40,000 to repair and refurbish a home after 10 years of occupancy.

> *$40,000 at the end of 10 years is not an uncommon outcome. I think most social housing providers would argue that that's about what they would pay for refurbishment at year 10. (Participant 3)*

Due to this substantial risk and expense, it was emphasised that make-good provisions were important as a means of providing investors with asset security: *'We do really prioritise some of the make-good provisions, because we know that is usually a concern for these types of investors'*. (Participant 2)

5.4.3 Targeting government schemes

Finally, there was general agreement that it was more effective to target government schemes to the not-for-profit sector rather than private sector investors, as this reduced the risk of private investors dropping in and out of ownership at the individual property level.

The volatility of the private investment market was seen to negatively impact long-term stock availability due to market and other conditions that impacted investment choices. However, the 'difficult middle ground' was identified as the need to find a balance between CHPs providing substantial quantities of housing stock, and private investors participating in the market in a carefully regulated way. Such a balance was needed to ensure that supply of housing stock could meet demand.

> *I would rather rely on an institutional investor. Like, I give the money to a CHP, the CHP goes and rents 100 units from a big institutional investor on a 10-year lease with indexation built in and rent prices built in. There's certainty for everyone. Relying on this market [small-scale investors] is very problematic for us. (Participant 1)*

5.5 CGT and negative gearing concessions

The quantitative analysis undertaken in this research project identified that approximately 4 per cent of investors were 'flippers'—that is, investors who purchased higher-end properties that they would sell quickly, and for a profit. These investors were motivated by profit rather than social benefits, and were incentivised by negative gearing and CGT concessions. It was recognised that these investors were not ideal in the affordable housing landscape, as they created a degree of instability and often subjected tenants to higher rental prices.

The workshop discussion focussed on whether it was helpful to continue to incentivise this group through tax concessions or other benefits:

> *The taxpayer is subsidising somebody's fifth and sixth investment property when there is a huge demand for social and affordable housing, and there are people struggling in the private rental market. So, I think from a purely equity pointy of view, I struggle with that. (Participant 1)*

However, it was noted that it was unlikely these tax incentives would be abolished, because of political pressure. At the same time, one participant stated that these incentives served a positive purpose, too; they bolstered housing supply and eased pressure on rental prices overall: *'If you try and disincentivise those people from operating in the market, you're putting upward pressure on rents, at least in the short-term'.* (Participant 5)

With this in mind, it was suggested that small tax policy changes (rather than wholesale tax policy changes) might benefit community housing. One such suggestion was to reduce the tax-free portion of CGT.

It was recognised that it was difficult to identify the tipping point between the costs and benefits of these incentives in creating optimum community housing outcomes. Also, this tipping point was not static—it changed based on the investors' personal circumstances and the nature of the market at the time. Again, the 'difficult middle ground' was required.

Given that these investors support an important, albeit small, segment of the housing market, conversation turned towards ways to incentivise them to support community housing goals:

> *[These investors] might be more willing to offer lower rents because they are being effectively subsidised by [CGT] concession and the negative gearing. (Participant 5)*

5.6 Awareness and education

The workshop participants noted that those investors who had been engaged in headleasing expressed high levels of satisfaction with the scheme. Despite this, there remains a low level of awareness of the scheme in the community. The type of investors who might engage in headleasing were identified as diverse and disparate, without a cohesive community or representative body that could be used to communicate with or educate them. Headleasing was identified as increasingly important, especially in Queensland and New South Wales where it is used extensively, as it allowed both expansion and flexibility in the programs that could be provided. Therefore, it was seen to be important to be able to communicate with and educate investors who might be attracted to headleasing arrangements. Social media marketing campaigns and local relationships were identified as effective ways to reach this group of investors:

> *When you are talking about how we get out to the potential investors, those local relationships between our staff, but also between the CHPs and the people that they know on the ground, are the most effective way to bring those investors in. (Participant 2)*

5.7 Policy development implications

Participant 3 summarised the findings of the workshops succinctly:

> *I agree that the CHP space is the most important at this point in time, with all of the different reforms. And I think if there's other sources of capital that want to get involved and can facilitate providing housing outcomes for those that are struggling to get into it under a normal market scenario, then we should definitely be open to it. (Participant 3)*

While it was recognised that the CHP sector played a vital role, and that it should be responsible for most of the affordable housing provided, it was noted that private investment increased housing stock and reduced pressure on rental prices. It is important that such private investment is carefully managed to ensure stability for tenants. CHPs expressed a clear preference for large-scale investors over small-scale investors. As such, the following policy recommendations are aimed at ensuring the optimal functioning of small-scale private investment in affordable housing:

- Small-scale investors can be supported to provide greater stability in the affordable housing ecosystem by:
  - ensuring make-good provisions protect the investor's asset
  - indexing rents on headleases to market rents
  - educating investors about the risks of investment to ensure they can weather financial hardships rather than sell up.
- Headleasing has been proven to be successful in New South Wales, Queensland and Tasmania. Headleases provide security and stability for both investors and tenants. However, the schemes are not well known to investors in all states. Awareness campaigns through social media and local networking could increase the take-up of headleasing.
- Small-scale changes to tax incentives, such as reducing the tax-free portion of CGT, could be used to incentivise investors to hold their properties longer, thereby creating greater stability for tenants.
- Overall, the preference is for government incentives to be directed to CHPs, who are seen to provide better long-term solutions. However, some private investment is needed to ensure adequate supply of diverse housing stock.

6. Policy development options

Nearly one-third (31%) of Australian households rent their residential dwelling (ABS 2021) and housing stress has become a critical concern, especially for low- and middle-income earners in the private rental market (AIHW 2021). The COVID-19 pandemic disproportionately impacted low- and middle-income earners and adversely affected their ability to afford private rental housing (Baker, Bloom et al. 2020; Oswald, Moore et al. 2020).

However, cost-of-living pressures post-COVID are forcing groups that could previously sustain private rental housing into the affordable housing market. Such groups include:

- essential workers (Gilbert, Nasreen et al. 2021)
- older Australians (Faulkner, Sharam et al. 2023)
- women (AHURI 2024).

Reynolds, Parkinson et al. (2024) have reported that more ‘rich’ households are turning to rental properties as housing prices increase, with households earning over $140,000 per year accounting for 24 per cent of renters in 2021, compared to just 8 per cent in 1996. These pressures combined in 2021 to create a shortfall of 348,000 affordable and available private rentals for households with the lowest 20 per cent of incomes.

Governments have used various policy levers, such as tax benefits or regulatory concessions, to incentivise small-scale investment in the supply of affordable housing—however, these measures have not achieved the required outcomes. For example, the NRAS delivered a little over half of the targeted 50,000 rental dwellings (Rowley, James et al. 2016). Small-scale investors comprise 90 per cent of all property investors in Australia and own approximately 23 per cent of all dwelling stock (Forbes 2021). However, our survey revealed that only 39 per cent of respondents were engaged in either the NRAS or headleasing. This indicates that there is scope to incentivise this group to consider the affordable housing market in greater numbers, thereby increasing the supply of affordable housing. With previous schemes having limited success, and an urgent need to address the affordable housing shortfall, new approaches are required to incentivise this group.

This project reviewed national and international evidence and conducted original empirical research in order to develop recommendations for policy mechanisms that could be applied to address the shortfall in small-scale investment in affordable housing. The following recommendations synthesise findings from our analysis, with evidence from the literature, and include policy mechanisms directed at different levels of government.

6.1 Policy mechanisms to increase small-scale investment in affordable housing

While small-scale investors are important suppliers of rental housing stock, policy and industry-side participants in our research acknowledged that this type of investment has its shortfalls. Small-scale investors were seen to come with risks. First, they can create instability in the market when they sell or increase rents; and second, they can be emotionally attached to their properties, seeing them as a personal asset rather than an investment.

Overall, policy makers and CHPs preferred that government incentives were directed to CHPs rather than small-scale investors, as CHPs were seen to provide more secure, long-term solutions and less instability for tenants. However, it was also acknowledged that CHPs did not have the capital capacity to provide an adequate supply of diverse housing stock. As such, effective policy measures must address the risk factors associated with small-scale investors.

6.1.1 How can financial incentives address cashflow impacts?

Approximately 46 per cent of investors in our survey ranked positive cashflow as the most important investment strategy; further, we found that the financial conditions of any scheme are the most important determinant of investor participation. Therefore, any scheme designed to attract small-scale investors should address cashflow incentives. Equally, existing government incentives and schemes that provide financial incentives that are not related to cashflow are unlikely to support small-scale investors entering the affordable housing market.

Financial incentives function differently for short-term hold investors and long-term hold investors.

Short-term hold investors

Short-term hold investors, or 'flippers', buy higher-end properties with an intention to sell quickly at an inflated price. This type of activity has the potential to destabilise the market, create tenant instability, and contribute to housing price and rental increases. It also puts pressure on the affordable housing market. Our analysis shows that around 4 per cent of small-scale investors are short-term hold investors—which means that this group does not contribute a significant amount of housing stock to the market. For these reasons, they are not the optimal investor type for affordable housing, and government incentives should not be directed at this group of investors.

Existing government measures that incentivise 'flippers' include negative gearing and CGT concessions. Our analysis shows that these measures provide very limited benefit to the affordable housing landscape—and have a detrimental effect by incentivising this group of undesirable investors.

Long-term hold investors

Long-term hold investors, who made up most of the investors in our survey, do not acknowledge any benefit in negative gearing or CGT concessions—instead, they see the purpose of their investment as providing positive gearing (cashflow), and intend to hold the property long-term. This group provide more stable housing and are much more likely to engage in long-term affordable housing schemes than 'flippers'. (Even if 'flippers' engage in the affordable housing market, it is usually for a very short timeframe.) For these reasons, long-term hold investors are the preferred target group for government incentives. To incentivise this group, schemes must earmark cashflow—for example, by reducing state government land tax. Based on our quantitative analysis, the average small-scale investor would need a tax offset (or equivalent) of roughly $650 per year for every 1 per cent market discount provided.

Investors in our survey also strongly value schemes that assure rental income over a specific period. Again, this reinforces the importance of positive cashflow to investors. All else being equal, investors are 12 per cent more likely to participate in a scheme that provides a rental guarantee. This provides investors with confidence that they can meet their mortgage repayments, thereby mitigating cashflow concerns. However, it is also important that rent is indexed to market rates so that investors are not disincentivised when locked into long-term schemes such as headleasing.

For schemes such as CRA to incentivise long-term hold investors, the level of assistance must be high enough to ensure higher rents can be charged. This will ensure that these landlords are positively geared, and thus less likely to have concerns about cashflow.

NRAS-like schemes targeting new supply would likely garner long-term engagement in affordable housing if monthly cashflow was assured. This could be achieved by indexing the guaranteed rental income to market rates and reducing land tax.

Deterring 'flippers' while incentivising longer-hold small-scale investors is likely to create a stronger, more stable affordable housing ecosystem. This will moderate house price and rental inflation and encourage greater owner-occupation and longer-term rental investment.

6.1.2 Can make-good provisions incentivise small-scale investors?

Headleasing involves the leasing of private rental accommodation by state housing authorities or CHPs, which then sublease these properties to approved households, usually social housing tenants. Headleasing is a form of non-owned strategic asset management. It is flexible and does not require upfront capital expenditure from the CHP. Headleasing is attractive to small-scale investors.

However, for headleasing schemes to be successful, make-good conditions are critical. Schemes must ensure that the property is returned to the landlord in the original condition at the end of the lease, thereby giving the investor confidence that their asset is protected. Make-good schemes can be expensive, with participants in our survey noting that on average $40,000 was required to restore a property to its previous condition at the end of a headlease.

It can be challenging for CHPs to acquire the capital to ensure that make-good provisions can be met. Some CHPs allocate a portion of rent for make-good provisions; others obtained the funds through government subsidies. Such government funding sources are viewed as being grossly underfunded.

The average investor in our sample would be 7 per cent more likely to participate in a scheme that offers make-good conditions than one that does not. Also, the average investor in our sample would be willing to give up about $7,150 in annual tax rebates if there was a make-good provision.

Related to these points, investors prefer schemes that allow them to lease to higher-income households. The average investor would require at least $2,400 in annual tax rebates to house tenants in an income bracket that is 10 per cent lower. This implies that investors are concerned that they are more likely to sustain property damage if they let their property to lower-income households—which will impact both their cashflow and the value of their investment.

Providing well-funded, sustainable make-good provisions that provide landlords with an effective guarantee that their property will be returned to them in the same condition it was originally let in will make headleasing programs highly attractive to long-hold investors.

6.1.3 How can effective communication and education be used to generate awareness and interest in small-scale investment?

Two issues arose in our analysis that can be addressed through communication and education programs.

Firstly, those investors who were engaged in affordable housing schemes found them highly satisfactory. Eighty-one per cent of investors rated their satisfaction level with their social housing scheme as either 'somewhat satisfied' or 'very satisfied'. Satisfaction with NRAS was higher, at 86 per cent, and headleasing had a satisfaction level of 71 per cent. However, despite these levels of satisfaction, there appears to be a low level of awareness of the schemes among investors.

Evidence from our qualitative research indicates that investors may not be aware of affordable rental housing schemes, but they express interest in participating when they do become aware of them. Analogously, our quantitative analysis demonstrated that between 40 and 60 per cent of investors in our sample would be willing to participate in schemes similar to NRAS or headleasing. Given that, of the 800 participants in our survey, only 312 (39%) were already participating in either NRAS or headleasing schemes. This represents an opportunity to engage a large portion of private investors in such programs. Coordinated national marketing and communications strategies could be developed to improve awareness of available schemes. Due to small-scale investors being highly dispersed and lacking central governance, an aggregator-model approach could be valuable.

Secondly, our qualitative analysis found that some long-term hold small-scale investors are naïve and make poor investment decisions. Due to a lack of financial literacy, they may overcommit to their investment. Then, when unexpected extrinsic factors occur, such as interest rate rises or extended periods without a tenant, they are impacted by financial hardship—which might lead to them selling their properties. This, in turn, creates disruption and potential rental increases for the tenant. Given the importance of ensuring that small-scale investors can provide stable, long-term housing, preferably while engaged in long-term headleasing programs, education of this cohort could filter out vulnerable investors. Alternatively, prudential regulations might also be applied to ensure these vulnerable investors do not enter the market.

6.1.4 Can policy lure STLs into the affordable housing market?

Holiday rentals through platforms such as Airbnb have attracted significant media attention because of their impact on housing availability. However, our survey showed that only 2.6 per cent of respondents rank holiday lets as their most important investment strategy. This implies that most small-scale investors are more concerned with buying properties that will provide long-term lets. This aligns with our qualitative interviews in which participants noted that STLs were undesirable because they were difficult to manage and came with additional costs.

Despite this, there are pockets of real estate, especially in popular tourist areas and high-density inner-urban areas of Melbourne and Sydney (Crommelin, Troy et al. 2018) that have high proportions of holiday rentals, and this can affect housing affordability in those places. At the same time, key workers on low-to-moderate incomes in these regions—for example, nurses, teachers, and emergency services personnel—are being pushed out of these high-density urban areas (Gilbert, Nasreen et al. 2021).

Key workers undertake work that requires a physical presence; they are not able to work from home. The combination of the high cost of housing in certain areas, a moderate or low income, and the need to live close to their place of work, means that key workers in large urban centres and some regional areas are particularly vulnerable to housing stress. Gilbert, Nasreen et al. (2021) reported that 49,000 key workers in Melbourne and Sydney were living in overcrowded homes, and 37 per cent were experiencing housing stress in these cities. Luring STLs away from holiday markets could create more affordable housing for key workers in these areas, as well as for others in need of affordable housing.

Tasmania is a jurisdiction that has had success in using headleasing to draw investors out of the STL market and into affordable housing. This was done using a combination of social and financial incentives. Social incentives appealed to investors' compassion, while financial incentives addressed the rental gap, tenancy management fees, rental guarantees, and covered property damage. While programs such as the Tasmanian model can be costly, a broad and comprehensive approach to funding headleasing schemes can be beneficial in areas where affordable housing is significantly impacted by STLs.

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