

How can shared equity schemes facilitate home ownership in Australia?

SMALL, WELL TARGETED SHARED EQUITY SCHEMES ARE ALREADY SUCCESSFULLY ASSISTING LOWER AND MODERATE INCOME HOUSEHOLDS TO ACHIEVE HOME OWNERSHIP IN AUSTRALIA. GOVERNMENTS HAVE HELPED CREATE THESE SCHEMES BY PROVIDING GUARANTEES, BUT THEIR LONGER TERM VIABILITY IS DETERMINED BY PROVIDING A PRODUCT CUSTOMERS WANT AND RUNNING THE SCHEME ON A SOUND COMMERCIAL FOOTING.

KEY POINTS

- There is consumer appetite for shared equity schemes in Australia, with particular interest in models that keep *normal home-ownership* within reach. For this reason, there is interest in schemes that allow the consumer to: *staircase* up to full ownership at a later stage; choose their own house on the private market (rather than be limited to particular stock); and capture equity gains by selling into an open market.
- Most of the shared equity schemes currently in place in Australia provide those features. Private sector institutional investors and lenders are interested in shared equity schemes, however private financiers remain cautious due to uncertainty and unfamiliarity with the product.
- Government-backed agencies have been instrumental in driving innovation and establishing shared equity schemes, especially in states with a good track record of affordable home finance provision. Governments have offered supports and government guarantees to facilitate the creation of these schemes, however they operate on a commercial basis.
- The fragmented nature of shared equity schemes across different jurisdictions suggests that there is a role for National leadership at a policy and regulatory level, and potential for state and territory government involvement in supporting government run schemes.

This bulletin is based on research by Dr Simon Pinnegar, Dr Vivienne Milligan, Professor Bill Randolph, Ms Dana Quintal, Dr Hazel Easthope, Mr Peter Williams and Professor Judith Yates at the AHURI UNSW-UWS and AHURI Sydney Research Centres. The research examined the appropriateness and potential for shared equity approaches to assist lower and moderate income Australians into affordable and sustainable home ownership. Shared equity arrangements are where the consumer shares the capital cost of purchasing a home with an equity partner.

BACKGROUND

The past decade has witnessed a growing level of concern over the affordability of Australian housing. Shared equity schemes are one option for addressing these concerns. These initiatives have the potential to facilitate home ownership for those households who may have difficulty purchasing a home through the open market.

Shared equity schemes vary in detail but broadly allow the consumer to obtain part equity in a home by sharing the overall cost with an equity partner—either a financial institution or a government backed provider. The involvement of an equity partner helps to reduce the overall costs involved in a mortgage, and thus improves housing affordability. Two different models are examined in this project:

- The *individual equity* model, which allows individual households to enter arrangements with equity partners in order to reduce mortgage repayments and the size of the deposit. At the time of sale, the partner recoups their equity loan plus a proportion of the capital gain. In some variants of this model there is an opportunity for households to *staircase* their way to ownership by progressively buying out their partner.
- The *community equity* or *subsidy retention* model, which preserves ongoing affordability by limiting the resale value of properties through the use of a predetermined formula.

Variants of the individual equity model are currently operational in most Australian jurisdictions. Private-sector led products, such as the *Rismark-Bendigo* scheme, have been launched. More substantive engagement has occurred in jurisdictions where *government-backed* but arms-length agencies, such as *HomeStart* in South Australia (SA), remain an integral part of local institutional and mortgage finance frameworks. The main government linked shared equity products are listed in the following table. All products are targeted towards lower

income households and subject to eligibility criteria. HomeStart's Equity Start (and Keystart's former Goodstart product) are specifically designed to enable public housing tenants access to home ownership.

This project sought to better understand the strengths and weaknesses of different shared equity models.

RESEARCH METHODS

This project involved obtaining information from existing and potential consumers, of shared equity schemes in two stages:

- A small number of interviews were conducted with existing shared equity customers from South Australia, Western Australia and the Northern Territory to explore their experiences of home ownership through such schemes.
- Ten focus groups were conducted with *potential* consumers in Sydney, Melbourne and Brisbane in order to explore consumer perceptions of different shared equity models. Both private and public renters participated.

In addition, interviews were conducted with institutional stakeholders—banks and lenders with an interest in innovative products like shared equity—in order to gauge interest and identify key opportunities and barriers to shared equity schemes from the perspective of the private sector.

FINDINGS

There is consumer appetite for shared equity schemes

- Existing consumers of shared equity schemes in Western Australia, South Australia and Northern Territory demonstrate the appeal of shared equity approaches. Schemes have allowed customers to purchase housing suitable to their household

| State | Provider | Shared equity products |
|--------------------|--|--|
| Western Australia | Keystart Home Loans | First Start (withdrawn 2009) Step Up Scheme (from 2010, consolidating previous Goodstart, Access and Aboriginal Home Ownership schemes) |
| South Australia | HomeStart Finance | Breakthrough Equity Start |
| Northern Territory | Territory Housing | HOMESTART NT |
| Victoria | VicUrban/ Burbank Homes | Ownhome |
| Queensland | Queensland Department of Housing | Pathways |
| Tasmania | Housing Tasmania | HomeShare |
| ACT | The ACT Affordable Housing Action Plan 2007 signalled a role for shared equity | |
| NSW | No current schemes | |

needs although many had to move out to areas where prices were more affordable. Being able to purchase through the open market was valued. Concerns focused on future uncertainty—for example understanding what happens when they come to sell or how they might meet obligations placed upon them in time.

- In focus group discussions, potential consumers also responded positively to the concept. Once explained, they understood shared equity as a concept and could articulate the benefits, recognise downsides and accept that trade-offs are involved. This suggests complexity may not be a key barrier to demand.
- Potential consumers distinguished between the individual equity model and the community equity model. They perceived the individual model as helping them become a *normal*, home owner, providing them with not only the security of ownership but with the potential of wealth creation.
- The community equity model is perceived as an affordable, secure housing option and seen more as: a 'good idea, but not for me'. Key reasons included that it was 'more like renting, but you're getting a proportion of the rent back at the time you move out'. There was no potential to buy the equity partner out, and consumers were limited in terms of choice within the housing market.

Institutional stakeholders and lenders are interested in shared equity schemes

- Lenders expressed some interest in shared equity and a number of interviewees reported that shared equity schemes represent a complex response to well-understood *market failures*. However interest was tempered with caution and concerns about the costs of bringing a new product to market and potential risks to reputation. Lenders also reported unfamiliarity and a lack of track records with these products.
- Uncertainty and unfamiliarity heighten risk. Lenders were uncertain if this market was going to be temporary while prices were high or a permanent market with temporary *residents* who move through to the mainstream market.
- Lenders noted potential problems arising from any divergence between house price and income growth on a borrower's capacity to buy out the loan. This might constrain normal market mobility.
- There was some concern that government involvement might unnecessarily complicate product development, but many lenders considered government participation appropriate as a means of *cushioning* added risks.

Government has played an innovative role in developing shared equity schemes

- Government initiated shared equity schemes have been well placed because they can benefit from cheap funds and Treasury guarantees. The lower cost finance enables them to innovate in this part of the market, including in directing products to those households that might be perceived as a greater risk by mainstream lenders.
- Central to the model is striking a balance between targeting support to those most in need, and sufficient freedoms to act as a commercial concern. Schemes need to ensure purchasers have the financial capacity to service the debt and need to be flexible enough to respond to changing market conditions. For example, if eligibility criteria are too loosely targeted, schemes may become oversubscribed. Alternatively, if eligibility criteria are too tightly defined to only permit a low maximum property value products become unviable—there may be no properties available at that price point.
- In Australia, government-backed schemes that operate at an arms-length from government, such as HomeStart Finance in South Australia, have been successful in achieving affordability objectives and maintaining financial viability. Key features attributed to this success include statutory independence, viable operating scale; staff and board members who are drawn from business and finance sectors rather than government departments; and close and trusting partnership with government housing departments and Treasuries.

Shared equity schemes need to consider market context

- Schemes should not simply enable access and purchase. Arrangements also need to relate to market context over the life of a housing loan.
- Housing market trends are not uniform across a state/territory or between and within cities. The design of shared equity products needs to take into account differences in incomes and house price characteristics across city sub-markets.
- Current schemes typically allow customers to purchase in the open market. In general, the market impact of such schemes is minimal, however for some dwelling types and popular first time buyer locations (with prices near the price maxima for schemes) there have been additional demand-side pressures at product launch.

POLICY IMPLICATIONS

- Shared equity models should be considered as one part of a strategic whole-of-housing policy approach which includes entry to home-ownership as an objective to ease pressure on other parts of the housing system—such as private rental housing. Shared equity arrangements should remain on a small scale, carefully targeted and positioned as one of a range of options.
- The open nature of many individual equity schemes currently on offer is in tune with consumer preferences for schemes that allow people to step up to home ownership and freedom to choose your own house. In this respect the present schemes are in tune with widely held norms and aspirations about home ownership.
- Purchasers need to have the long-term financial capacity to service housing related debt. Therefore targeted eligibility criteria are important. Schemes need to be geared towards those with incomes below, but not significantly below, median incomes and enable purchase of properties in the lower quartile to median price range. Shared equity schemes should not be driven by a policy to assist those in most housing need.
- This may raise concerns regarding *middle class welfare*. The subsidy helps beneficiary households build capital gains rather than preserve affordability in the housing stock. By contrast, those schemes that do preserve affordability, such as community equity schemes, have received less interest to date and appear less favoured by consumers. This presents a dilemma for Governments that wish to seek a greater long term affordability dividend for its investment.
- Shared equity schemes have yet to get a substantial track record in the eastern states. This is partly because of the negative experiences with low start loans schemes in the early 1990s. Arrangements where potential risk at the establishment phases are shared between Commonwealth and states,

and a national education campaign targeted at both consumers and industry, would serve to alleviate fears about the risks involved.

- Addressing the disparity in access to shared equity arrangements across jurisdictions is a challenge. Extending the reach of the agencies currently administering schemes outside the realm of their own jurisdictions, risks undermining their strengths gained from alignment of funding, responsibilities and local knowledge of their own jurisdiction markets. A national scheme, administered by Canberra, risks undermining those schemes already in place and would struggle to replicate the conditions that state based agencies can provide.
- There is room for national involvement to provide long-term commitment and greater certainty, for example through consistent taxation and regulatory frameworks for all parties involved. That commitment needs to be considered in terms of the contributory role appropriately targeted schemes can play in helping deliver the aims and objectives of the National Affordable Housing Agreement. A national framework in support of financing arrangements would also help provide scale, help spread location risk across different housing markets and enhance cost effectiveness.

FURTHER INFORMATION

This bulletin is based on AHURI project 70394 *Innovative financing for home ownership: the potential for shared equity initiatives in Australia*.

Reports from this project can be found on the AHURI website: www.ahuri.edu.au

Or contact the AHURI National Office on +61 3 9660 2300

www.ahuri.edu.au



HEAD OFFICE Level 1, 114 Flinders Street Melbourne Victoria 3000 TELEPHONE +61 3 9660 2300
FACSIMILE +61 3 9663 5488 EMAIL information@ahuri.edu.au WEB www.ahuri.edu.au

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