SUBMISSION

Affordable Housing Working Group Issues Paper

The Council on Federal Financial Relations

Solving the simultaneous housing equation:

An innovative and practical proposal to unlock capital markets and increase the supply of affordable, social and private housing

March 2016

Executive Summary

The crisis of housing affordability in Australia has become one of our nation's most pressing public policy challenges. We thank the *Affordable Housing Working Group* for the opportunity to make a contribution to this important discussion.

When analysing the problem of housing affordability, we must at all times remind ourselves of the housing continuum. There is one housing market in Australia and interventions in one sector of the market will almost inevitably impact upon other sectors, for better or for worse. A key factor making housing unaffordable is a lack of housing supply. It is not the only factor, but it is a significant one.

Therefore, a holistic approach to improving housing affordability in Australia must seek to increase the supply of all forms of housing: private, affordable and social. This is particularly the case as a more robust long term solution requires tenants to graduate through this housing spectrum.

In order for an affordable financing model to succeed it must unlock three fundamental challenges simultaneously. We call these challenges the *simultaneous housing equation*. The challenges are:

1. Governments need to be willing to provide increased funding, guarantees, or land/stock transfer;
2. The community housing sector needs to be credible at managing and increasing affordable and social housing stock at a very large scale; and
3. Capital markets need to be unlocked through appropriate risk-adjusted returns.

There have been countless well developed affordable financing models put forward over recent years. We trust that many more will be submitted to this Working Group. The challenge with all proposals that we have considered and engaged with is none simultaneously solve each key challenge.

A fundamental truth of any discussion surrounding affordable housing financing is that in order to facilitate the free flow of capital from the private sector, the shortfall of income relative to market based levels needs to be solved by government intervention in one of three ways: directly providing large amounts of government funding, guaranteeing debt used to finance affordable housing, or providing land/housing stock which can be leveraged.

The proposal we put forward for the establishment of a new innovative financial clearinghouse solves all three key challenges simultaneously. We have built on previous proposed models of issuing affordable housing bonds, as identified in *Model 1: Housing loan/bond aggregators* discussed in the *Issues Paper*. However, where such proposals have relied on government funding subsidies or guarantees, we have developed a model which leverages existing state and territory government land to fund the construction of new affordable and social housing dwellings.

Additionally, we provide a framework for the facilitation of scaled housing construction activities creating a pipeline of projects, a necessary requirement of any debt market solution.

Finally, our model results in a more efficient aggregation of capabilities based on the essential core competencies of the providers.

Our proposal to establish a Commonwealth Affordable Housing Clearinghouse (CAHC) will provide an innovative solution to unlock capital markets and facilitate significant investment in the development of affordable and social housing in Australia. This can be achieved in an efficient and a cost effective manner.

The CAHC will facilitate the development of large housing construction projects which will produce private, affordable and social housing. Private housing development profit margins effectively are retained within the non-profit structure and will cross-subsidise the development of affordable and social housing by contributing to debt principal and interest payments. This allows highly rated debt securities to be issued to capital markets. Affordable and social housing will be transferred to Community Housing Providers (CHPs) and state and territory government housing authorities.

This proposal provides a holistic solution which increases the supply of private, affordable and social housing across Australia at scale. This approach improves housing affordability in the private market in addition to providing targeted affordable and social housing, while providing a significant economic stimulus through large scale housing construction.

The separation of major construction activities and bespoke tenancy and management services is an important benefit of the CAHC. To maximise efficiency, construction activities are best delivered by large private sector contract builders, allowing CHPs and state and territory housing authorities to focus on their core competencies of tenancy management and service delivery, while benefiting from growth through stock transfers from the CAHC.

Additionally, the development of such an innovative financial clearinghouse would allow for consideration of further financial innovation aimed at unlocking capital markets, such as the issuance of social impact bonds.

This fit-for-purpose solution will solve the simultaneous housing equation; allowing governments to increase affordable and social housing without major capital expenditure or debt guarantees, and unlocking capital markets by providing appropriate risk-adjusted returns. Perhaps most importantly, it allows CHPs to focus on their core business: providing housing and support for those most in need.

1. Background

Australia faces a housing affordability crisis.

The 2016 Demographia International Housing Affordability Report revealed that Australia is one of the most unaffordable housing markets in the world. All Australian major metropolitan areas[1] are classified as 'severely unaffordable' and Australia's largest city, Sydney, is now ranked as the second most unaffordable city in the world after Hong Kong[i].

If mortgage repayments form more than 30 per cent of a household's disposal income the household is said to be under mortgage stress. Most Australian households currently face mortgage stress. The latest REIA Adelaide Bank Housing Affordability Report (December 2015) revealed that Australian households' average mortgage repayment's now make up 31.7 per cent of the median family income[ii].

Despite substantial federal, state and territory government investment in social and affordable housing in recent years, notably through the *Nation Building - Economic Stimulus Plan* and the *National Rental Affordability Scheme (NRAS),* hundreds of thousands of Australians currently languish on public and community housing waiting lists.

Australia currently provides slightly over 400,000 social housing dwellings (including public, community and indigenous housing)[iii], while around 190,000 Australian households sit on public and community housing waiting lists[iv].

Thus, Australia requires an almost 50 per cent increase in social housing simply to meet current demand and provide housing for those seeking it. This is an immense public policy challenge for all levels of governments.

While the authors acknowledge that the focus of this *Issues Paper,* and our submission to it, emphasises financing models for affordable housing, we stress the nature of the housing continuum (as aptly represented in Figure 1 of the *Issues Paper*). There is one housing market in Australia. Government interventions in any market segment are almost certain to impact all segments of the housing market.

The existing supply shortfall in Australian housing will only be exacerbated by long-term population and demographic trends. Most commentators suggest that the current supply pipeline will temporarily narrow the supply-demand gap in the next few years[v], but overall population growth and increasing longevity will ensure demand for new housing continues to put pressure on the supply pipeline.

The ABS estimates that Australia's population will rise from its current level of 24.0 million to between 36.8 and 48.3 million by 2061, due to increasing fertility and continued net overseas migration[vi]. Population growth of over 50 per cent in the next generation and a half will sustain strong housing demand and is likely to reinforce the supply shortfall. NSW alone is projected to require an additional 694,000 dwellings over the next 15 years[vii].

Increasing longevity will further stimulate demand. Not only do longer lives drive population growth by reducing mortality rates, they result in declining average household size (household fission): more older people, particularly women, live alone, meaning that more dwellings will be required in future to sustain any given rate of population growth. The ABS projects that the lone-person households will be the fastest growing household type over the period 2011-2036 with growth between 61 per cent and 65 per cent, equating to 1.3 million new households[viii].

[1] A major metropolitan area is defined as a city with a population greater than 1 million.

Longer lives influence the demand for social and affordable housing in additional ways. The average age of social housing tenants is increasing and tenures are becoming longer. This shift creates demand for a different type of dwelling: age-friendly housing units where design is informed by the mobility and amenity needs of older residents, often living alone.

In recent years First State Super, Per Capita and the authors in numerous capacities have initiated and participated in a range of discussions seeking to identify financing models to support the provision of additional social and affordable housing. These discussions have included, but not been limited to: federal, state and territory government ministers, departmental and agency heads, institutional investors, CHPs, property developers, representative industry groups and associations, business leaders, academics, government and non-government policymakers and expert consultants. These discussions have assisted us to identify the challenges we discuss and informed the development of our proposed framework.

2. Challenges

This submission concurs with the *Issue Paper's* identification of specific factors influencing housing affordability such as restrictive land use policies and the challenging risk-return profile of affordable housing. However, additional challenges permeate almost every aspect of affordable and social housing policy which contribute to the complex challenge identified.

We believe that the flaw in numerous well developed financing proposals is that they address some, or many, challenges but not all of them. Due to the interdependent nature of these challenges, any financing proposals will ultimately be unviable unless all key challenges are simultaneous addressed.

Overview of the three key challenges

i. Government challenges

- Budgetary pressures have seen public investment in new housing slow, with supply no longer being able to meet increasing demand as evidenced by increasing waiting lists;
- The significant implicit subsidies provided to social housing users (up to 55% of market rent) have largely been underfunded. Reductions in maintenance spending have seen housing stock "run down" over time and a large proportion of the housing stock in need of substantial refurbishment;
- Long social housing waiting lists are reflective of both chronic undersupply and the increasing tenure of tenants. Increasing tenure is likely to be in part due to a lack of affordable housing options;
- The shortfall between rental collections, operations and maintenance costs is growing, placing further pressure on state and territory governments' finances and further reducing their ability to free up funds to invest in new housing stock;
- As the average age of stock increases, maintenance costs are increasing and the quality of housing provision is declining; and
- Despite ageing and deteriorating housing stock, state and territory governments are reluctant to initiate large-scale stock transfers as public housing is often the second or third largest asset on government balance sheets.

ii. Community Housing Providers (CHPs) challenges

- The community housing sector lacks meaningful scale both in aggregate and as individual providers;
- Community housing comprises 18 per cent of Australian social housing resenting 72,000 dwellings managed by approximately 45 CHPs[ix];
- The community housing sector is highly fragmented, with the largest providers representing only a small fraction of total stock (approx. 5,000 dwellings);
- Comparatively, the largest single CHP in Britain manages approximately 70,000 dwellings, while the largest fifteen providers manage approximately half a million homes[x];
- *Due to a lack of scale, CHPs are required to simultaneously increase their stock through obtaining finance, undertaking in-house development and project management activities, while ensuring appropriate tenancy management and delivery of social services and programs;* and
- As a result of these challenges, there is considerable scepticism amongst state governments as to the ability of CHPs to absorb large scale stock transfers and/or develop large volumes of stock themselves.

iii. Capital Markets challenges

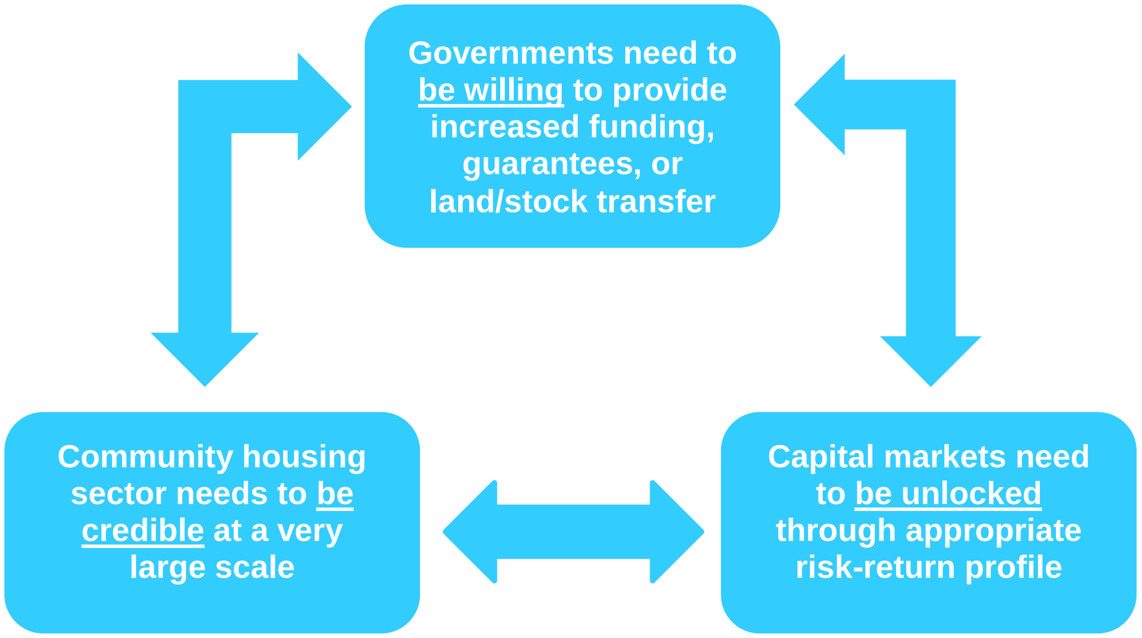
- Australian capital markets, increasingly dominated by our growing $2 trillion superannuation savings pool, are often suggested as a source of funding for affordable and social housing projects through various iterations of Public-Private-Partnerships (PPPs);
- Superannuation funds are required by the Australian Prudential Regulation Authority (APRA) to hold high levels of liquid investments which can be redeemed at short notice by fund members to move to another fund or drawdown during retirement;
- Any form of direct property investment through PPPs, joint-ventures or property syndicates and trusts are highly illiquid investments;
- The current environment of low/zero real yields in traditional defensive assets, in conjunction with relatively full valuations in growth assets, has meant that funds need to maximise their return from their illiquid portfolios;
- Affordable or social housing provides a lower rental yield than alternative property investment options (retail, office & industrial), while a heavier reliance on capital appreciation, as commonly embraced by private residential investors, is relatively less attractive;
- Furthermore, institutional investors have been unable to access benefits of negative gearing or capital gains tax concessions that individuals, who effectively set the market price, can enjoy;
- Illiquid investments which provide relatively low yield, in a market priced by retail investors who are subsidised through government tax exemptions, do not provide attractive investment opportunities for institutional investors in their existing form; thus
- Ultimately, the volume of bank lending (which is currently relied upon for the limited development projects undertaken by CHPs) is constrained and would not be sufficient to enable meaningful changes in housing supply of this type. Capital markets financing through traded debt issuance will be required.[2]

[2] In the last two years, by way of example, non-government bonds issued in Australia amounted to close to $20bln per annum. Outstanding non-government bonds on issue are over $500bln.

Addressing the three key challenges simultaneously

Unless the three key challenges of government willingness, community housing credibility and capital markets risk-return requirements are simultaneously addressed in a meaningful and substantive manner proposed solutions will fail. The authors have encountered numerous proposals that address one or two of these challenges – but none that successfully address all three simultaneously.

Figure 1 – The simultaneous housing equation



3. The fundamental truth of government involvement in any affordable housing solution

Before proceeding to outline our proposed model, it is vital to clarify a fundamental truth of government involvement in any solution that seeks to increase the supply of affordable and social housing in Australia in the current environment.

By its very definition, providing affordable and social housing through discounting market rental rates will never provide the returns that investors operating under fiduciary obligations will require in isolation. An investor's required return (the minimum return an investor requires given an asset's risk profile) will always be higher than the return affordable housing will be able to provide in isolation. A fiduciary investor, operating under our existing regulatory framework, is simply not able to accept rental payments of 80% of market rent from a tenant, facing all the associated investment risks of renting out property, when they could accept 100% of market rent elsewhere.

Therefore, when examining how institutional investors' capital might be directed into affordable and social housing investments, there will always be a *'return gap'* which is the difference between the required return demanded from investors and the return discounted market rental properties will yield.

This return gap must be met by government[3]. Any proposal that proffers a solution without acknowledgement of this fundamental truth (and preferably identifying how the return gap should be met) is in our view flawed.

There are broadly three ways that governments can (and currently do) meet this return gap:

1. Through directly providing government funds/subsidies/grants;
2. Through a government guarantee of outside investors' capital; or
3. Through government provision of land/housing stock for the purposes of development or redevelopment.

It is widely accepted that neither the Commonwealth Government, nor any state or territory government, are countenancing substantial recurrent government spending aimed at developing affordable and social housing. This is a view the authors do not dispute.

Similarly, there have been numerous proposals (similar to Model 1 in the *Issues Paper*) that have proposed the issuance of affordable housing bonds backed by a government guarantee. Briefly, such bonds which would provide a lower return then a similar asset in the private market (the return gap), would have investment risk reduced through a government guarantee to pay interest and principal payments. This would make the lower return provided acceptable to investors. Despite such proposals being widely canvassed for over a decade, the authors are unaware of any level of government that has favourably considered such a proposal. Therefore, we do not propose any government guarantees in our model.

Our proposed model relies on the government provision of land (currently used for affordable/social housing or additional land) which will allow mixed private, affordable and social housing development. The private housing proportion will be sold (or potentially rented for some period) at market rates. The development profits from these transactions subsidise the affordable/social housing, meeting the return gap. Further detail is provided in Section 5 and the Appendix.

[3] This gap could in theory be met through philanthropic commitments. However the scale of the investment required compared with Australia's historic levels of philanthropic contributions suggest such a possibility is so highly improbable that it warrants no further consideration at this time.

The notion of using development margins (made available through the provision of land/dwellings and some type of increase in density) is not new and is a proven model[4]. The challenge, however, is to deliver it at a sufficiently large scale to make a meaningful difference to social and affordable housing supply.

4. The objectives of a successful affordable housing model

We believe that *Model 1: Housing loan/bond aggregators* proposed in the *Issues Paper,* and several affordable housing bond proposals put forward in recent years[xi] provide the appropriate framework for an affordable housing finance solution. However, we believe that such proposals have not addressed all of the key challenges outlined in Section 2. Specifically they have not: 1) met the return gap without a government guarantee; or 2) identified how the scale of development required to create a new asset-backed/secured bond debt market could be achieved.

Before detailing our proposal to establish a Commonwealth Affordable Housing Clearinghouse (CAHC) in Section 5, we believe there are five objectives that any successful affordable housing financing model must achieve. These are:

- An investment mechanism that provides market-based returns commensurate with its liquidity and risk;[5]
- Large scale, diversified and institutional grade development projects involving a mixture of private, affordable (and potentially social) dwellings;
- A development pipeline to provide the required volume of projects for investment; and
- Institutional grade counterparties delivering development projects and arranging financing.

i. <u>Investment mechanism</u>

Following extensive consultation and modelling, the authors believe that a form of Affordable Housing Bonds (AHB) provide the most attractive investment mechanism for institutional investors to finance affordable housing. Our proposed model, detailed in the following section, would not require a government guarantee.

Investors require lower rates of return from such liquid securities compared to illiquid direct investments. This allows institutional investors such as superannuation funds who have liquidity requirements to invest in such securities. Further, AHB's can be structured (see Box 1) in such a manner that a high proportion of bonds attract a high investment grade credit rating; ensuring both initial investment and a liquid secondary market for the bonds.

Such bonds would indicatively be generated through the following steps:

Step 1: Debt finance required to fund the development of a mixture of private, affordable and potentially social housing would be pooled together, facilitated by a central entity.
Step 2: This central entity would then create bonds which pay both interest and principal based on the underlying debt pool. We envisage there would be two tranches within the bond structure – an equity (or first-loss) tranche and a senior tranche.[6]

[4] It is being used as part of the NSW Government Communities Plus programme, in addition to being commonly relied upon by CHPs at small scale.
[5] Creating a structure that has improved liquidity reduces the required rate of return and, in so doing, makes the model more viable.

Step 3: Private dwellings developed as part of the pool of housing would be sold to reduce the debt pool.
Step 4: Affordable and social housing stock would be transferred to CHPs or state/territory authorities.
Step 5: Rental returns (including Commonwealth Rent Assistance where applicable) from affordable and potentially social housing are used to pay interest and repay principal debt.

ii. **Scale and density**

The largest financing of a community housing development project in Australia to date has been Westpac's financing of $61 million to Australia's largest CHP St George Community Housing to build 275 new homes[xii]. This was an innovative and impressive partnership to be commended.

However, in order to conduct one successful issuance of AHBs a minimum underlying debt pool of around 10 times that amount ($600 million) would be required. As is clear from earlier discussion of Australia's housing affordability crisis, issuances of this size are absolutely required to address the pressing supply shortfall, however Australia's community housing sector does not have the scale and expertise to deliver such projects.

The facilitation of large, diversified, institutional grade property development projects is where government participation is required and forms the basis of this submission's proposed solution.

A successful $800 million issuance of AHBs could finance the development of approximately 23,000 new homes, including 10,000 affordable and social dwellings (see Appendix example). Currently even a large alliance of Australia's leading community housing providers would not have the capacity or capability to deliver such a project. However, an innovative central entity, as proposed in the following section, would be capable of delivering projects of such scale.

Such an entity would be designed to have the scale and expertise to contract leading property building companies to deliver private and affordable mixed housing construction projects which would be financed through the issuance of AHBs. Upon completion, private dwellings would be sold and affordable housing transferred to CHPs and/or the relevant state/territory housing authority.

Density

A necessary component of greater scale is the increased density of the housing developments. The proposal put forward in Section 5 meets the *return gap* through the development and subsequent sale (or rental) of housing into the private market.

A piece of land containing sparsely developed social housing would be re-developed increasing the development density of both affordable/social housing (realising a net addition of affordable/social dwellings) as well as private housing.

This increase in density provides a dual benefit which will improve housing affordability in Australia. Firstly, the development profits from the new private housing (which are retained within the financing entity) are used to cross-subsidise the development of affordable and social housing, meeting the *return gap* identified.

---

[6] The purpose of the equity tranche is to increase the rating of the senior tranche and so facilitate greater interest from debt capital markets while improving liquidity.

Secondly, as discussed in the *Issues Paper* and this submission, the housing market continuum is such that additional supply of private housing puts downward pressure on both the cost of owning and renting private housing in addition to renting affordable housing.

The creation of additional private housing supply improves housing affordability in its own right. When used to support the development of targeted affordable and social housing – a dual benefit is realised.

iii. Pipeline volume

While a successful single issuance of AHBs would be a fantastic achievement, the long-term viability of such a financing model requires the development of a liquid market. The development of a pipeline of projects would allow the financing entity to undertake AHB issuances on a semi-regular basis improving the breadth and depth of Australia's asset-backed/secured bond debt market and capital markets in general.[7] Additionally, the development of a strong pipeline of housing projects provides additional economies of scale further enhancing the risk-return profile of the securitized assets.

iv. Institutional grade counterparties

The final critical component of any successful affordable housing financing model is the involvement of institutional grade counterparties. The underlying housing development projects funded by the AHBs must be constructed at scale by large credible builders or syndicates. This will help to ensure that the AHBs achieve the appropriate credit ratings and meet the required risk-return profile for institutional investors.

Property development is a high risk activity. Investors of all sizes will bear such risk if they are provided with appropriate expected returns. As has been discussed, affordable housing development alone will not provide these returns. Therefore such projects must be 'de-risked' as much as possible through large, diversified projects, secured through transparent competitive tendering processes, undertaken by institutional grade property development companies or syndicates and overseen by development experts.

Box 1 - Asset Backed or Secured Bonds

Asset-backed or secured securities are bonds or notes backed by financial assets. These assets consist of receivables which can include credit card receivables, car loans or mortgages.

A financial institution originates the loans such as a bank, credit card provider, consumer finance company and turns the loans into marketable securities. The loan originators are commonly referred to as the issuers, but in fact they are the sponsors, not the direct issuers, of these securities.

These securities or bonds are then sold to investors who receive the specified coupon (interest) payments and the principal payment at the bond's maturity.

In this case, we envisage that the bonds would be secured against the social and affordable housing cash flows, and that repayments would be a mix of principal and interest.

[7] A further ancillary benefit of this proposal is the provision of greater diversity and depth in Australian debt markets.

5. Commonwealth Affordable Housing Clearinghouse (CAHC)

The establishment of a Commonwealth Affordable Housing Clearinghouse (CAHC) would provide an innovative solution to meet all of the canvassed objectives. It would unlock capital markets, facilitating significant investment in the development of affordable and social housing in Australia in a cost effective and efficient manner.

A successful CAHC could take many forms and evolve in a range of different manners. This submission provides an overview and framework for consideration, discussion and further investigation. A modelled project case study is provided in the Appendix.

Objective The CAHC will finance and develop housing stock to be transferred to CHPs and/or state and territory housing authorities. The CAHC will not manage affordable or social housing.

Establishment The CAHC will be established as an innovative new statutory authority with the Commonwealth Government as the majority shareholder and each state and territory government as minority shareholders.

Personnel The board and management of the CAHC would comprise of individuals with expertise in property development, capital markets and institutional investment. The omission of individuals with community housing expertise is deliberate. The CAHC is not a CHP, nor should it seek to become one or in any way displace CHPs. The purpose of the CAHC is to support the growth of CHPs through developing and then transferring housing stock to CHPs.

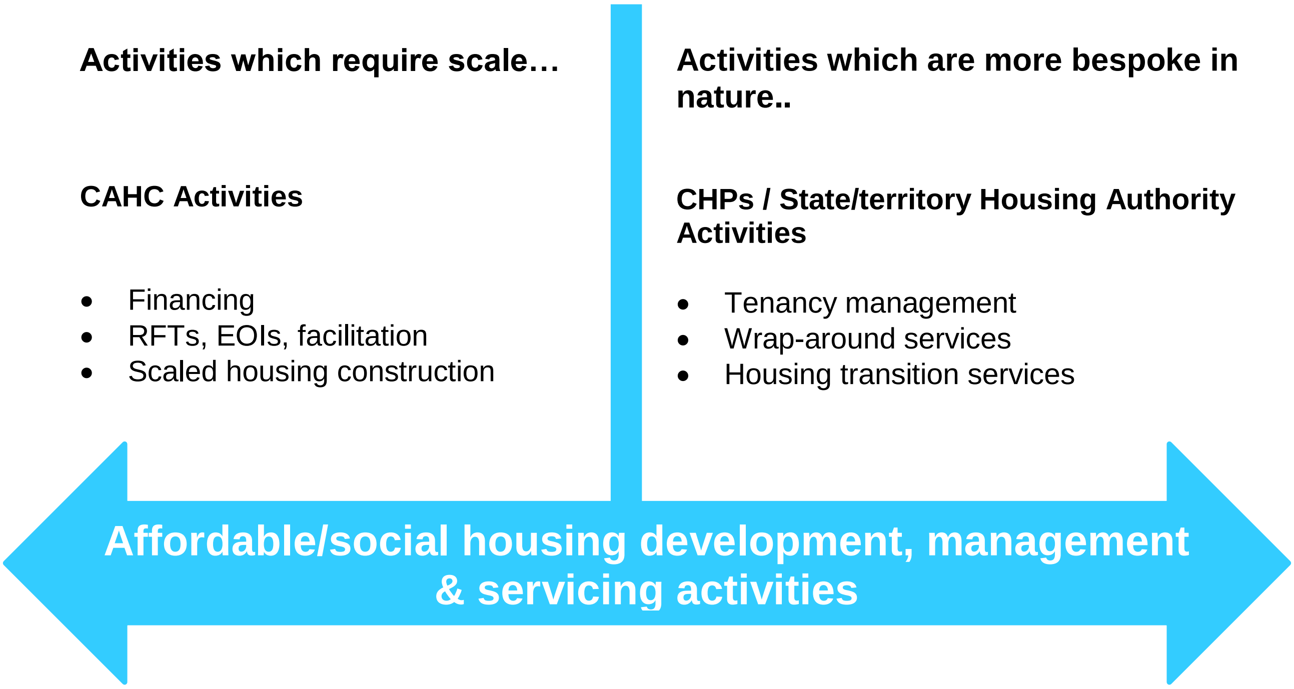
Project structure The CAHC would act as a central expert facilitator and clearinghouse for the development of affordable housing nationally. The CAHC will partner with state and territory governments, CHPs and builders to generate housing construction projects which will produce affordable housing stock. State and territory governments (as well as potentially the Commonwealth) would provide government owned land for development (in the case of greenfield sites) or redevelopment (in the case of brownfield sites). The CAHC, in partnership with the relevant state or territory government, would issue tenders to leading residential building companies for the construction of private, affordable and social housing dwellings. Additionally, the existence of such a central entity could help to secure planning approvals for affordable housing projects deemed to be of significance in conjunction with the appropriate state or territory planning authorities.

Debt Issuance The CAHC would facilitate the issuance of project debt.

Stock transfer Following the successful development of affordable housing stock, the CAHC would transfer this housing stock to the appropriate CHPs or state or territory housing authority as determined by the relevant state or territory government. Transfers to CHPs could be in the form of a long term lease with beneficial ownership reverting to the relevant state or territory government.

Management The CAHC's sole ongoing management responsibility following the completion of a housing project would be to ensure that AHB holders receive interest and principal payments. The CAHC would work with state or territory governments through existing monitoring mechanisms to ensure that properties are being maintained, tenanted and rental income is received. The CAHC may benefit from economies of scale by engaging central maintenance contractors to oversee maintenance of housing stock while the stock is servicing the AHBs.

Figure 2 – Fit for purpose affordable and social housing

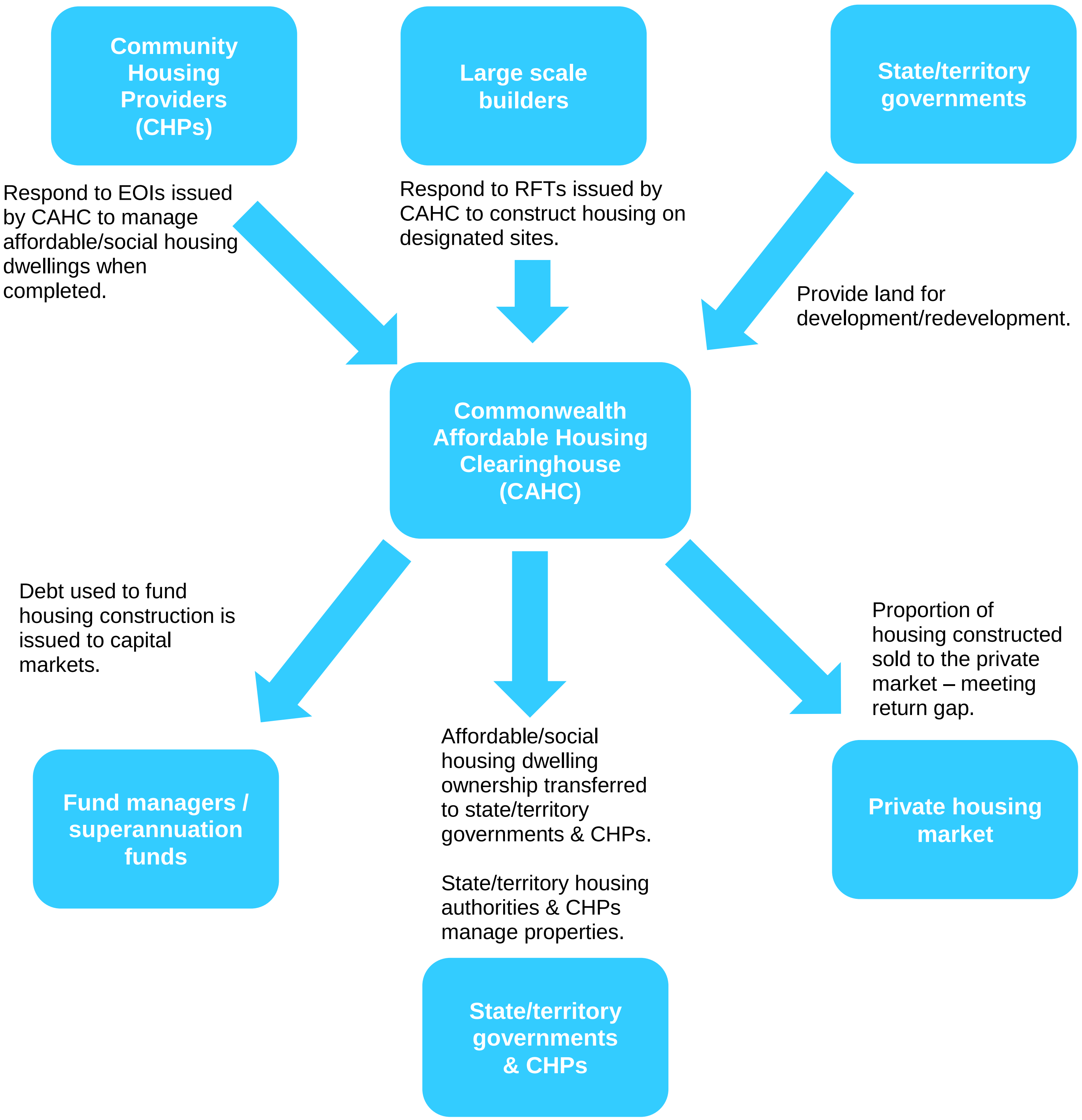


Benefits of the CAHC

Some noteworthy benefits of the CAHC model that are often not addressed in other models include:

- Providing an innovative financial mechanism to unlock capital markets – facilitating investment in affordable and social housing;
- Improving the efficiency of private, affordable and social housing development through large scale development in partnership with institutional grade builders;
- A separation of scaled development activities best delivered by large private sector builders, and bespoke tenancy and management services best delivered by CHPs and state and territory housing authorities;
- *This separation of activities (detailed in Figure 2) facilitates growth of CHPs while allowing them to focus on their core competencies of tenancy management and social service provision;*
- Through increasing the density of housing on land provided by state or territory governments, this proposal leverages this land (through private housing development) to subsidise the affordable and social housing construction. This allows the *return gap* to be met without requiring significant monetary contributions or debt guarantees from governments. Additionally, the required density increase can be altered based on the amount of land/dwellings state or territory governments transfer;
- The ratios of private, affordable and social housing can be altered based on differing interest rate and inflationary environments, ensuring the model is viable throughout the business cycle;
- A holistic solution which increases the supply of private, affordable and social housing across Australia at scale. This approach improves housing affordability in the private market, in addition to targeted affordable and social housing dwellings; and
- The development of such an innovative financial clearinghouse would allow for consideration of further social investment opportunities such as the issuance of social impact bonds.

Figure 3 – The Commonwealth Affordable Housing Clearinghouse (CAHC)



6. Conclusion

For decades, Australia has failed to build enough homes to meet demand.

This lack of housing supply has increased the cost of buying or renting a home. Families and individuals that once could afford to purchase their own home have been pushed out of the housing market and into the private rental market. This increase in private rental demand has put upward pressure on rental costs. Many individuals and families, particularly key workers on inflexible incomes such as nurses, teachers and police officers, can no longer afford to rent in the private market and must seek subsidised affordable housing. Many Australians require additional support, as almost 200,000 sit on social housing waiting lists. Others fall into homelessness; living in squalid and overcrowded accommodation, couch-surfing or sleeping rough.

There is only one Australian housing market – and a fundamental component of any plan to improve housing affordability must include a significant increase in housing supply. This submission's proposal, if implemented, would result in a step-change in housing delivery across Australia in private, affordable and social housing.

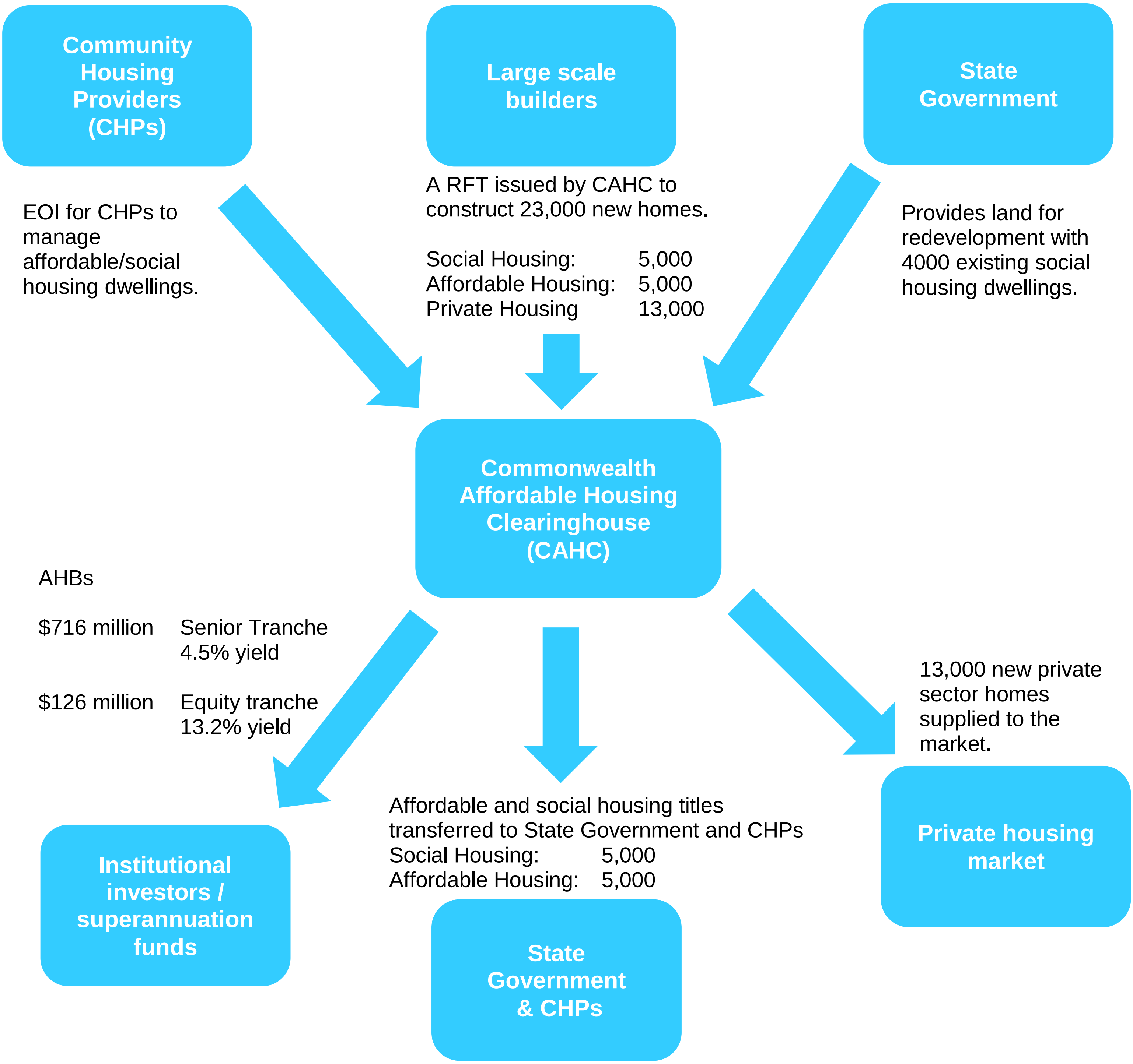
Numerous considered and well developed financial proposals have been put forward with the goal of increasing the supply of affordable and social housing in Australia. In recent years many have congregated, rightly in our view, around the concept of affordable housing bonds as canvassed in Model 1 of the *Issues Paper*. However, none of these models have adequately solved all three of the key challenges in the simultaneous housing equation (Figure 1).

The establishment of a fit-for-purpose Commonwealth Affordable Housing Clearinghouse (CAHC) solves the simultaneous housing equation. Governments will be incentivised to provide land and housing stock in order to achieve greater levels of stock at no cost and without being burdened with debt guarantees. Capital markets will be unlocked as investors are provided with appropriate risk-adjusted returns subsidised through the development and sale of private housing. Finally, the community housing sector will be provided with increased housing stock to manage while being liberated from building and development activities. This will allow CHPs to focus on their *raison d'etre*: providing bespoke social and tenancy services and, if appropriate, working with tenants to transition into other forms of housing.

Appendix

The following is a modelled Case Study of how the CAHC could operate. The authors are currently in the process of undertaking detailed modelling of the CAHC which can be provided to the Affordable Housing Working Group upon completion.

Figure 4 – A CAHC Case Study



This case study would result in a **net increase of 19,000 new homes** comprising of 13,000 new private dwellings, 5000 new affordable dwellings and 1000 new social housing dwellings. The existing 4,000 social housing dwellings would be replaced with new stock.

Assumptions - CAHC Case Study

Inputs	
State Government stock transfer	4,000 dwellings
Outputs	
Social Housing	5,000 dwellings
Affordable Housing	5,000 dwellings
Private Housing	13,000 dwellings
Total Housing delivered	23,000 dwellings
Net Increase in dwellings	19,000 dwellings
Costs and Values	
Cost per dwelling	$275,000
Total development cost	$6,325,000,000 ($6.3 billion)
Completed value per dwelling	$450,000
Total development value on completion	$10,350,000,000 ($10.3 billion)
Loan to Value Ratio (LVR)	61%
Original land value per dwelling	$250,000
Development margin	41% (accrued to CAHC)
Rental Yields	
Residential market yield	5%
Affordable discount	75%
Affordable Yield	3.75%
Social Discount (inc. CRA)	36%
Social Yield	1.8%
Income	
Social Income	$40,500,000
Affordable Income	$84,375,000
Total Income	**$124,875,000**
Principle reduction from private sales	$5,850,000,000
Initial Debt	$6,325,000,000
+ one year interest (5.8%)	$6,691,850,000
Net Debt (after sale of private)	$841,850,000
Ongoing Interest	$48,827,300
Tenancy management & Maintenance (28% of income)	$34,965,000
Total Expenses	$83,792,300
Straight Line amortisation p.a. for 30 years	$28,061,667
P+I+Maintenance	**$111,853,967**
Interest Cover	*x1.1*
Debt Issuance	
Bond Value	$841,850,000
Attachment Point	15%
AAA Tranche	$715,572,500 Yield 4.5%
Equity Tranche	$126,277,500 Yield 13.2%
Yields	
30 Yr Govt Yield (implied)	3.8%
Margin	2.0%
Total Interest Rate	**5.8%**
Senior Tranche Margin (AAA/AA Rating)	0.7%

About submission authors

First State Super

Richard Brandweiner, CFA, Chief Investment Officer, First State Super

First State Super was established in 1992 to provide for the superannuation and retirement needs of NSW public sector employees and their families.

Since that time, we have opened our doors to all Australians, becoming one of the country's largest super funds with more than $53 billion under management and over 755,000 members. We are a not-for-profit fund and therefore run only to benefit members. In addition to superannuation, life insurance and retirement products, we have more than 50 financial planners who can offer affordable advice on a range of superannuation and boarder financial matters.

Per Capita

David Hetherington, Executive Director, Per Capita

Per Capita is an independent progressive think tank dedicated to building a new vision for Australia based on fairness, prosperity, community and social justice.

Per Capita's research is rigorous, evidence-based, and long-term in its outlook, considering the national challenges of the next decade rather than the next election cycle. We ask fresh questions and offer fresh answers, drawing on new thinking in science, economics and public policy.

The Committee for Sydney – Financial Services Knowledge Hub

Peter Bentley, The Committee for Sydney – Financial Services Knowledge Hub

The Committee for Sydney was appointed by the NSW Government in 2014 to identify and coordinate actions of the Financial Services Knowledge Hub. The Financial Services Knowledge Hub is a platform for sharing best practice, identifying new opportunities, for advocacy and collaboration, both across the private sector and between the private and government sectors.

Submission contact

Peter Bentley

Ph. 02 9345 1129
Email peter@uictoria.com

References

[i] 12th Annual Demographia, International Housing Affordability Survey 2016 (2016)
[ii] Adelaide Bank/ Real Estate Institute of Australia Housing Affordability Report (2015), '*Housing affordability declines over the September quarter'*, (http://www.adelaidebank.com.au/news/2015-news-articles/copy-of-housing-affordability-improves-over-june-quarter)
[iii] The Council on Federal Financial Relations (CFFR) Affordable Housing Working Group (2016), *Affordable Housing Working Group Issues Paper*, p.4 (http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2016/CFFR-Affordable-Housing-Working-Group)
[iv] Productivity Commission 2016, *Report on Government Services 2016 Chapter 17*.
[v] See QBE Insurance (Australia) Ltd (2015), *Australian Housing Outlook 2015-2018*, QBE: Sydney, Chart 16 (https://www.qbe.com.au/~/media/qbe/files/about-qbe/industry-insights/j7031-australian-housing-outlook-report-20152018.pdf)
[vi] Australian Bureau of Statistics (2013), *3222.0 Population Projections Australia, 2012 (base) to 2101*, ABS: Canberra (http://www.abs.gov.au/ausstats/abs@.nsf/mf/3222.0)
[vii] NSW Department of Planning & Environment, *2014 NSW Household and Dwelling Projections Data*, NSW Government: Sydney (http://www.planning.nsw.gov.au/en/Research-and-Demography/Demography/Population-Projections)
[viii] Australian Bureau of Statistics (2013), *3222.0 Population Projections Australia, 2012 (base) to 2101*, ABS: Canberra (http://www.abs.gov.au/ausstats/abs@.nsf/Latestproducts/3236.0Main%20Features42011%20to%202036?opendocument&tabname=Summary&prodno=3236.0&issue=2011%20to%202036&num=&view=)
[ix] NSW Federal of Housing Associations Inc (2016), (http://www.communityhousing.org.au)
[x] The G15 London (2016), (http://g15london.org.uk)
[xi] Australian Housing and Urban Research Institute (2012), *Housing Supply Bonds - a suitable instrument to channel investment towards affordable housing in Australia?* (http://www.ahuri.edu.au/research/final-reports/188)
[xii] Community Housing Coalition of Western Australia (2014), *Westpac signs its largest Community Housing Provider deal,* (http://commhousing.com.au/westpac-signs-its-largest-community-housing-provider-deal/)