

Council on Federal Financial Relations

Affordable Housing Working Group

Response to the January 2016 Issues Paper

Submitted by: The Porter Davis Group

March 2012



Respect the dream

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1. Introduction

This submission has been prepared in response to the Issues Paper circulated by the Affordable Housing Working Group and its call for interested parties within the housing industry to respond with ideas and proposals to help address this pressing matter.

Porter Davis Homes is one of Victoria's leading project home builders constructing over 1,500 homes each year and with a turnover in excess of \$500m p.a. In 2012, Porter Davis was proud to be selected as one of three builders chosen to partner with the Victorian State Government in the regeneration of the Geelong suburb of Norlane.

It was Porter Davis's first experience of working collaboratively with the Victorian Government and the project not only resulted in the delivery of well over 100 new public housing units, but also in generating a significant level of private investment by the participating builders in delivering affordable new homes for private purchasers in an area which, in the past, had been sadly neglected by the market.

In addition to the Norlane project, members of the senior management team at Porter Davis have previously gained firsthand experience in the establishment of significant collaborative public/private affordable housing projects in Kensington (Vic) and Bonnyrigg (NSW) in partnership with the Victorian and New South Wales Governments respectively. Porter Davis are currently working on an innovative project with Women's Housing, a not for profit Housing Agency that provides much needed accommodation for women fleeing family violence.

These initial collaborations, particularly in the renewal of older public housing areas, has led our company to proactively research the potential to expand our involvement in this sector. Porter Davis believes that the ageing condition and in particular the chronic underutilisation of much of the older family sized public housing stock in Melbourne's middle suburbs as well as in the other Capital cities offers a unique opportunity for Governments to partner with the Project Home Building Industry to cost-effectively address many of the issues as well as the escalating maintenance liabilities common to public housing providers in all Australian States. In the case of Victoria, these problems were graphically illustrated and identified by the State's Auditor General in his March 2012 Report 'Access to Public Housing'.

This submission takes a 'detached observers' look at some of the broader structural and financing issues that have, to date, hindered the development of a sustainable affordable housing sector that is now recognised as being so necessary to development of healthy, liveable and efficiently functioning communities into the future.

2. A 'Detached Observers' Overview of current issues

What we at Porter Davis understand by the term 'Affordable' housing for the purposes of this submission.

Porter Davis sees there being two areas of the residential 'rental' market that, in terms of delivering more sustainable and liveable cities into the future, need to be urgently addressed by Governments at State and Federal levels.

- i) The first, and the one which is the primary focus of both this submission and Porter Davis' interests as a company, is the sector that is generally described as either **Public and/or Social Housing** i.e.: the sector that is comprised in Victoria's case by the Director of Housing (DHHS) together with Community Housing sector i.e.: both Housing Associations and Housing Providers.
- ii) The second area is sometimes known as '**essential worker housing**' and is not a primary focus of this submission but is one that is becoming increasingly urgent to address as roads and public transport become increasingly clogged and as first home buyers and increasingly family renters are pushed to find homes further and further away from their preferred locations. This is an important sector in most European and US cities as well as in Asian cities such as Singapore. This sector provides long term rental apartment accommodation for lower but often middle income families to enable them to live closer to city centres and their areas of employment (and in doing so to make other 'non property' choices about how they invest for their futures).

2.1 Public and Social Housing

The Victorian Auditor Generals 2012 report clearly set out the key problems facing this sector in terms of rising and changing demand, underutilisation of stock, ageing stock leading to escalating maintenance liabilities and a chronic 'underfunding' of the sector leading to stagnant stock levels in spite of some limited renewal and redevelopment projects with capital assets often having to be sold to support recurrent management and maintenance costs.

From our observations when Porter Davis was involved in the redevelopment of housing in Norlane, one of Victoria's most disadvantaged suburbs, managing public housing is a very tough 'gig', particularly in areas where it is concentrated in relatively high densities and the majority of tenants rely on Government pensions or support for most of their income. In the case of Norlane, it was Porter Davis' observation, however, that with dedicated staff, and an albeit local redevelopment vision in place, some outstanding redevelopment and community renewal outcomes could be achieved.

Based on figures from the Auditor General's Report, the public housing asset base of 63,000+ units (out of a total affordable housing asset base of just over 80,000 in Victoria) can be broadly divided into four components, namely:

- High Rise Apartment Buildings, largely constructed between 40 and 50 years ago (7,000+ units)
- Medium Rise apartment buildings with some new additions but mostly 'walk-ups' constructed over 40 years ago (15,000+ units)
- Medium Density Terrace Homes (many built in the last 30 years (15,000+ units)
- Lower Density detached and duplex homes (26,000+ units)

The growth of the Community or Social Housing sector is itself also largely dependent on Government funding. The sector is comprised of only eight Housing Associations and around thirty plus Housing Providers. While some agencies do have some advantages in being able to operate more flexibly in connecting tenants with high support needs with those supports and some specialise in specific areas (i.e.: the aged homeless where Wintringham provides an outstanding service), the sector is generally underfunded and still largely reliant on Government for support.

In addition, while it could be said that the Director of Housing and the Social Housing Agencies operate in the same space and respond to the same client group, the reality is that this is far from being a level playing field. Tenants of the Housing Agencies are able to access Commonwealth Rental Assistance and the Agencies are also able to conduct their development (and other) activities in a GST free environment. Accordingly, any comparison of financial performance between DHHS and Social Housing Agencies is fraught with difficulty.

If any future overall restructuring of the affordable housing sector is to be both effective and sustainable, then it needs to be based on the clear recognition that there will always be a gap to close both between the capital cost of delivering new stock and any potential rental stream for debt servicing, and also between market and even subsidised rents and the capacity of tenants living largely on Government support to service their rental obligations. Accordingly there will always be a need for some form of rental subsidy or income support to close the rental gap and some new financial structures and or incentives to desirably attract new capital into the delivery of new stock. It is only in the area of leveraging the asset value of some parts of the overall public property portfolio that any significant opportunity exists to leverage the value of existing assets to renew and grow stock to any significant degree (see some of the suggested Victorian opportunities in the next section of this submission).

In the immediate future, while it is understood that the matter of growing the Social Housing sector by transferring management responsibilities for some public housing stock to the sector, and possibly in the future also transferring ownership is being actively considered, the reality remains that the Social Housing agencies are essentially very small scale operations. Even the larger Associations often have only a couple of thousand

properties without sufficient scale to free themselves of almost complete dependence on Government funding. Accordingly, a very real risk in any future incremental transfers of stock is that the short term outcome will simply be a depletion of the Governments (DHHS's) asset base and the 'fattening up' of a number of commercially sub-optimal 'mini' DHHS's in the form of the Agencies who, while they may be able to introduce some innovation or added value by using the CRA and GST advantages they enjoy, they will still be largely dependent on Government funding and support.

In conclusion, a key observation that Porter Davis would make in regard to the Housing Agency sector is that many of the larger players already see themselves as having a role as a 'hands on' developer as well as being the owner/manager of affordable rental stock. In bringing future efficiencies into this sector it would seem to us that some basic business management principles could be applied across the sector so that in the future each of the key player/stakeholders in the sector focuses on the area in which they have the greatest capacity and expertise to both manage risk and deliver outcomes. In other words a clearer division of responsibilities and a reduction in overlapping activity and duplication in the longer term might see a future Affordable Housing Sector being based on the following clearly defined split of responsibilities:

- **Expanded Housing Agencies:** Tenancy and property management and coordination of tenancy support, asset maintenance along with some property ownership but with, initially, most property continuing to be held on long leases from Government. Leases that are structured to allow for borrowings and approved redevelopment (with CRA and GST efficiencies);
- **Private Home Builders:** Project management and delivery of new stock including all permit processes up to handover;
- **Government:** Regulatory and performance frameworks for agencies, and Tax and Fiscal initiatives and regulation, ownership of leases and approval of redevelopment of programs for leased assets.

2.2 Essential Worker Housing

It is worth noting that many of the major public housing areas that were developed in Melbourne and other capital cities in the years after WWII effectively fell into the category of 'essential worker' housing at the time. For example the suburbs of Norlane and Broadmeadows were both developed in the period between 1945 and 1965 to provide housing for the large workforces recruited to new factories of the Ford motor company and International Harvesters established in those suburbs at that time.

Since then, the nature of public housing has been undergoing a major shift from being primarily housing for working families (including new migrants) to being housing that is increasingly required for those who are largely dependent on Government support including

people on disability and aged pensions, and people with complex needs and supports including the victims of family breakdown and new migrants and refugees.

As our cities have grown and property prices and demand for the better services available closer to city major regional centres has increased, however the capacity of employees on often reasonably good salaries to secure longer term accommodation with reasonable reach of their employment is becoming increasingly difficult. While land costs mean there is not likely to be any affordable solution to this issue involving full home ownership, there is a need for the development of a housing sector that can offer longer term security for families and smaller households than is currently available from the private rental market. Currently the apartment rental market is comprised primarily of individual investors most of whom would not agree to the types of long term renewable leases that are available in those countries where a regulated longer term private rental sector has been developed. In these countries the creation of purpose specific private or not for profit agencies have brought scale to the sector and new developments often involve investment by Superannuation funds or major corporate investors seeking secure underwritten returns that offer perhaps just 1% or 2% over the cash rate. Development capital to create new stock is then mobilised by the private sector into new projects with either tax credits and/or long term concessional leases of publically owned land.

As has been indicated earlier, this long term apartment rental sector is not a primary focus of either Porter Davis or this submission, but as a company committed to quality and liveability in our cities and one, that like many others, has employees that are increasingly impacted by crowded public transport and congested roads, we see initiatives such as this that will bring us into line with growing cities elsewhere in the world as being an important issue on which to make comment.

In the first thirty to forty years after the war, new low density suburbs of family homes became a hallmark of the Australian lifestyle, but now some of the costs of those lower densities are coming home to roost. More to the point we have recognised that we now live in a society where over 60% of households in the Metropolitan area comprise either only one or two people. The initially slow response to this new demographic from both the housing and development industry as well as our planning regulators has now been overtaken by an explosion in demand for apartment living and smaller homes matched with demand for better and more varied recreational and open spaces and more active and vibrant streets and urban areas.

In recent years Melbourne, perhaps more than most Australian cities has responded to these new realities and delivered both levels of growth and a 'liveability' and quality of life that make it the envy of many. Now, however, we face the challenge of how to sustain that quality and to secure it into the future by ensuring that it becomes more affordable.

3. Some Current Opportunities

As we indicated earlier the introduction to this submission, the management team at Porter Davis have had significant experience in working collaboratively with Government to deliver new projects which have not only been designed to grow the stock of new public housing units, but also to create more integrated local communities by also delivering new affordable private homes as part of the same overall projects.

This was the case at Norlane; one of Victoria's most disadvantaged suburbs where along with two other home builders over 160 new public units have been constructed alongside a similar number of new and very affordable private units. At Bonnyrigg in a larger project involving the private and not for profit sectors working with Housing NSW, and based on the renewal of a predominantly public estate of some 833 homes is now underway. The project objective is to achieve the wholesale renewal of those 800+ public units within a new replanned and reinvigorated and integrated community that will eventually comprise over 2300 new homes both public and private. Key players involved in negotiating and establishing that project are now part of the Porter Davis team.

In reviewing how we might further expand our collaborative work with Government, Porter Davis have undertaken a lot of work to see how new innovative renewal projects can be developed that can be driven primarily by leveraging the value of existing, but often old and underutilised assets to create value and expand the supply of affordable rental housing.

Porter Davis recognise that State Housing Agencies in Australia, while lacking significant levels of capital for new construction, face two key challenges today in respect to much of their older family sized housing stock i.e.:

- How to **renew** their low-density public housing assets; and
- How to **deliver new** affordable public housing to meet ever-growing demand from some of our society's most vulnerable citizens.

In Victoria, Porter Davis believes it has devised a simple and elegant solution that will help the Victorian DHHS address both the above issues – at minimal risk and cost to Government and is currently preparing a separate proposal which will shortly be submitted to the Victorian Government for consideration. We also believe that a similar approach would be likely to be applicable to public housing stock in other Capital cities.

Overall we believe our solution will deliver a minimum 15% uplift in public housing stock along with:

- Rejuvenated and integrated public/private/social housing precincts;
- Much-needed smaller units to replace older and underutilised family stock;
- Sustained net asset values for Government owned stock;
- A wider range of housing options for DHHS's ageing residents;
- More efficient use of DHHS land and assets;
- A reduction in future maintenance liabilities associated with older stock;
- A supply of new sites for affordable private homes in established suburbs.

Porter Davis believes that there are other opportunities for State Housing Authorities to leverage higher value parts of their overall portfolios to secure new developments that will both renew and grow stock without a significant requirement for new capital.

In Victoria for example, the Victorian DHHS manages the largest residential property portfolio in the State and by and large, while significantly underfunded, keeps most of it maintained and fit for purpose on an ongoing basis which is a significant achievement.

That portfolio includes a number of very high value sites in outstanding and desirable locations where there are clear opportunities to leverage the value of the site to secure new but in some cases smaller replacement units either on the same site or in other locations of the Departments choosing.

The key problem with leveraging asset value to secure new product is that while it will result in a reduction in maintenance liabilities (i.e.: new for old), it will always be seen by some as a sell down of the Governments assets notwithstanding that it should in most cases be possible to retain the Governments overall asset value once redevelopment is completed.

The following are examples of key large high value sites in Victoria where we believe that joint partnership projects between the Government and the private sector could yield new and possibly increased levels of public stock within an integrated public/private development:

- 1) **Ascot Vale** where the DHHS owns some 900+ largely 1 and 2 bed units in older low rise apartment buildings on a 17 hectare site which could comfortably accommodate a significant level of new development (3000+ units) without the need for expensive high rise construction. This inner city location would be well suited to an integrated public/social/private housing development and is close to public transport and shops.
- 2) **Barak Beacon Estate** is a public housing estate of some 70+units that is adjacent to the successful Beacon Cove waterfront development. The site could accommodate a significant increase in density with replacement public units either being delivered on site or on one of the many other relatively lower density public housing estates in the Port Melbourne area.
- 3) **Gardeners Creek Park** in Hawthorn, this very high value location currently accommodates around 50 small ageing units but has the capacity to provide for several hundred new apartments in a premium park side location and an opportunity to not only replace existing unit numbers but grow them significantly.
- 4) **Oakover Road Preston** - An existing post-war estate of some 25 duplex units on a site which has the capacity to accommodate over 200 new apartments (in low rise buildings) and 20+ terrace homes together with some parkland.
- 5) **Boston Place and Rae Streets North Fitzroy** - This site currently accommodates some 70+ units taking up much of a whole residential block in North Fitzroy and could sustain a significant increase in density in a premium inner city location.

4. The Changing Context

In this section we briefly outline our views on the changing policy, market and financial contexts in which both Government and Community Housing Agencies are operating and which in the coming years will need to be taken into account in any future endeavour to establish an enduring, sustainable and appropriately targeted affordable housing sector that adequately addresses the wide diversity of needs that are out there in the community.

While there are a wide number of factors currently impacting on how the affordable housing sector is evolving at the current time, three of the most significant issues are:

- 1) **The Growth of the Community Sector.** While the number of larger Housing Associations (8) is relatively few as compared to the number of Housing Providers (34), the dynamics within the sector are a little more complex. In particular, while even the larger Associations have only 2 or 3 thousand units and annual turnovers seem to be reflect the fact that these organisations generally lack the scale to be major player who might attract investor interest into the private market. On the other hand, some of the Housing Providers are agencies, often connected to Churches, which operate across a wide range of community support activities and in many cases often have a scale together with balance sheets and turnovers that dwarf those of any of the Housing Associations. In some cases i.e.: Baptistcare and the Salvation Army, these agencies are embarking on an active expansion of their interests and assets in affordable housing sector. While Government has taken the view that it would like to see the size of Housing Association grow (possibly by amalgamation) to achieve scale, it has in part sought to do this by restricting the number new Associations that are created irrespective of the scale of their balance sheets. We are not sure this restriction on new entries into the field is wise as it potentially impacts on the ability of larger new players to enter the field.
- 2) **The Roll Out of NDIS.** While the roll out of the National Disability Insurance Scheme is still in its early stages and the degree to which funding will be available either directly or indirectly for accommodation for people that receive an NDIS package, it is clear that there are likely to be some 'flow on' and also possibly some more direct impacts on the affordable housing sector. The shortage of appropriate accommodation for people with a disability is well known and has led to the situation where young people are sometimes having to be cared for in facilities designed for the aged. At the same time there are a very large number of people with a disability who live at home often with ageing parents and carers who, while they may be on a waiting list for a place in a community residential unit or a supported care facility, have little prospect of reaching the top of 'wait list'.

Once individual support packages are received and there is greater clarity about the degree that those packages can include rental or even loan repayments, then there is the prospect of a significant amount of funding coming into potentially new market

place, where home builders and not for profit service providers might collaborate in providing new accommodation with varying levels of support to a new group of renters or purchasers. These newly 'empowered' clients under the NDIS model will in many cases bring with them additional income or support from a family wanting to provide ongoing security of accommodation and a measure of independence to their disabled family member. It is still too early to say just how this potentially very significant part of the 'affordable' or supported housing market, is going to unfold in the coming years.

- 3) **Growth and Change in the Aged Care Sector.** The growing aged care sector together with the rise in the numbers of concessional beds in aged care facilities as well as the growth in specialised retirement living developments and new products to enable older home owners to release equity in their homes are all likely to have some impact on the affordable housing sector. The fact that in many areas, upwards of 30% of family sized (3br+) public housing stock is occupied by either a single elderly person or elderly couple over 65 is an indication of the degree to which much of the often ageing public housing asset base across Australia is significantly underutilised.

In concluding this section on the changing context we would also like to make the observation that in some cases there are changes in context that make the task of both companies like our own as well as other agencies wishing to engage with Government particularly frustrating. There appears at times to be a seemingly constant culture of change within Government accompanied by the lack of a clear and consistent pathway to take new ideas and initiatives to the relevant decision makers. To outsiders it seems that areas such as DHHS and the Office of Housing are subject to a seemingly unending round of reorganisations involving the creation of new units and policies and an ever changing parade of new faces to be briefed, updated or lobbied on any given issue. While there are notable exceptions, the general view is that it is very hard to determine who to go to submit new ideas or proposals and also to know either who will evaluate them or who is able to make decisions, and accordingly the default position usually becomes....try to see the Minister.

5. In Summary

- **If Governments at all levels are serious about establishing an affordable housing sector that can attract capital from the private or superannuation industry into the delivery of new stock then that system must have as a minimum the following characteristics and capabilities:**
 - * Governance through long term and consistent policy settings together with an ongoing commitment from Government in order to provide confidence to the market in relation to risks and management etc.
 - * A new purpose specific agency related to the above i.e.: “An Affordable Housing Finance Corporation” (AHFC) which can offer to support and provide part finance or tax credits (a purpose designed form of corporate negative gearing credit to attract investors) to suitable approved projects and ensure interest costs as well investment returns to investors are kept at levels that do not defeat the ‘affordability’ objective of the exercise i.e.: the equivalent of cash options in a super fund + 1% or 2%.
 - * A consistent approach to the offering of both suitable surplus Government sites for redevelopment for a mix of public/social and private housing as well as existing housing sites in need of redevelopment in lieu of always chasing ‘highest and best use’ on the open market with approved suitable sites (approved by AFHC on advice from relevant State Planning agency) qualifying for the finance or tax credits noted above.
- Development proposals that get approved for funding must come from established housing agencies or providers in collaboration with established/reputable builders or developers and there must be water tight provisions to ensure that the affordable rental component of the project remains as affordable rental. This could be achieved in the case of formerly State /Government land by the affordable rental component being retained in freehold by the State/Government and then leased on a very long lease to the housing agency for management, CRA etc.
- **If new Housing Agencies are to develop with sufficient scale to operate in this space and secure private funding and, in time, take over the current stock and tenancy management roles played by the State Housing Authorities then either existing community agencies need to grow and or amalgamate or other agencies need to emerge. These could be new entities coming out of the services management sector or they might be existing agencies or organisations that currently have a focus in another area such as aged care but which have the scale and balance sheets to transition into the affordable housing sector.**

Finally, the team at Porter Davis would urge all Governments and in our particular case, the Victorian Government, to actively review and act upon the wide range of opportunities that already exist to renew and better manage their ageing and underutilised housing stock.

We stand ready to enter into an innovative collaborative partnership with both Government and the not for profit sector to renew and grow the Departments lower density housing stock in particular. At the same time we would welcome the chance to discuss and expand on any or all of the issues we have raised in this paper as we at Porter Davis believe that the right to access an affordable home, whether you are a renter or a purchaser is an important cornerstone of a just and sustainable community.