A Plan for Industry and Government

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Property Council of Australia
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Improving Housing Affordability in NSW

A Plan for Industry and Government

The Voice of Leadership

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Housing affordability is now at its worst level in nearly 20 years. Despite relatively low interest rates, escalating house prices mean that average families are now spending more of their income on mortgage payments than when interest rates were 17 per cent in 1989. House prices have increased so dramatically that Sydney housing is more expensive than New York, London or Vancouver. In Sydney, 37 per cent of family income is required to pay the average mortgage. No wonder most 15-30 year olds believe that home ownership will not be affordable in their lifetime.

Improving the affordability of housing is essential in combating social problems – homelessness, poverty, unemployment, crime, family instability – but it is also an economic problem. Key workers – vital to a diverse and competitive economy – are being priced out of the housing market. Lack of affordable housing options for hospitality workers, transport operators, sales assistants, hospital workers, cleaners, carers and others may diminish the economic competitiveness of Sydney into the future.

Clearly, the existing policy approaches to improving affordability have failed. It is time for new policy reforms and an industry-government partnership to improve housing affordability. Sydney’s economy depends on it.

affordability snapshot

- Average house prices relative to income have almost doubled in 10 years.
- Average monthly payments on new loans have risen by 50 per cent in 10 years.
- Affordability is worse today than it was when interest rates hit 17 per cent in 1989.
- Sydney housing is more expensive than New York, London or Vancouver.
- In Sydney, 37 per cent of family income is required to pay the average mortgage.
- New home loan size is increasing faster than earnings or inflation.
- Nationally, over 750,000 lower-income households are in ‘housing stress’.

- Nationally, public housing stock is in decline, maintenance costs have skyrocketed and 200,000 people are on waiting lists.
- Home ownership is falling and permanent or long term renting has increased.
- Rising household debt means many are vulnerable to economic change.
- Mortgage default rates have doubled in three years – 13 houses a day in NSW are being repossessed.
- The IMF and the OECD warn Australia’s high house prices pose a risk to economic stability.
- Demand for housing is rising, keeping upward pressure on prices and rents.
- Government levies and compliance costs now make up 35 per cent of the cost of homes in Sydney’s north-west and 28 per cent of the cost of new units.
### Summary of Recommendations

- **Increase land supply**
  Strategically plan for the release of land by setting national, state and local targets; fast-track the release of land in Sydney’s Growth Centres and land out of these centres; benchmark to always have 15 years land supply; and audit surplus government lands and release these for affordable housing projects.

- **Invest in strategic planning**
  Implement the Sydney Metro Strategy and improve its links with infrastructure delivery; set up an Urban Renewal Commission to revitalise key areas and facilitate consolidation; streamline development assessment; and use voluntary agreements with developers to provide affordable housing.

- **Lower taxes**
  Reduce the cost of land development by cutting property taxes; fund infrastructure through debt borrowing, not levies; phase out stamp duties to promote home ownership; and exempt land tax for key projects.

- **Boost savings**
  Target the First Home Owners Grant (FHOG) to the needy; establish low deposit home loans; explore savings incentives such as nest egg accounts, matched savings accounts and early access to superannuation; encourage equity partnerships and offer key worker housing subsidies.

- **A role for the federal government**
  Affirm a role in our cities and re-establish the housing ministry; boost Commonwealth-State Housing Agreement (CSHA) funds for private investment in affordable housing; encourage the Future Fund to invest in privately financed affordable housing projects and create a sister fund to invest in social infrastructure, including affordable housing; offer National Competition Policy style payments to the states for reforms that improve affordability.

- **Initiate a bond scheme pilot study**
  Issue government bonds to the private sector to raise funds for investment in affordable housing by offering a ‘guaranteed minimum’ after tax return, targeting lower income earners and potentially assisting over 150,000 households per annum.

- **Initiate a securitised housing trust pilot scheme**
  The trust would finance affordable home ownership for low-middle income earners. A rental contribution from the occupant and a $30 million per annum contribution from government can generate $840 million in housing assets.

- **Increase the role of the community housing sector and private enterprise**
  Invest in upskilling the community housing sector, allow them to be more entrepreneurial in their activities and transfer public housing to the private sector for management and redevelopment.

### Affordability Today

Despite relatively low interest rates, strong economic growth, rising incomes and easier access to mortgage finance, the cost of housing is still relatively high compared to other periods in our history and affordability remains a pressing social and economic concern.

House prices have increased so dramatically in the past decade that Sydney housing is more expensive than New York, London or Vancouver.\(^7\) In trend terms, house prices have increased regardless of high or low interest rates. Average house prices relative to income have almost doubled in 10 years and average monthly payments on new loans have risen by 50 per cent, or around $500.\(^3\) Whilst there is some evidence that affordability has improved since 2003, the recovery in some markets, rising interest rates (eight interest rate rises since May 2002) and increasing debt levels means that for many affordability is now worsening.

Nationally, over 750,000 lower-income households spend more than 30 per cent of their income on housing and are deemed to be in ‘housing stress’.\(^6\) There are also 450,000 households in the private rental market in housing stress. This is particularly acute in NSW, where more broadly 37 per cent of family income is required to pay the average mortgage.\(^8\) Contrary to its original purpose, public housing is now targeted to those who are welfare dependent and not merely low income earners. Overall public housing stock is in decline, the maintenance costs have skyrocketed and it is estimated that 200,000 people nationally are on waiting lists.\(^7\)

House prices and the size of new (and existing) home loans have risen substantially in the past few decades, far outpacing earnings, income or inflation.\(^4\) According to the Reserve Bank of Australia, affordability is worse...
today than it was when interest rates hit 17 per cent in 1989.13 Mortgage interest payments now account for 9.1 per cent of all household disposable income, up from the 6 per cent peak in 1989.10 Debt repayments overall now require 11 per cent of household income to service, compared to 9 per cent in 1989.12 Affordability is particularly worse for new home owners. In 1989, when interest rates were 17 per cent, 25.8 per cent of household disposable income was needed to repay the average new home loan. Today, it is 28 per cent of household income.13 Ownership is falling and permanent or long term renting has increased.14 Indeed, as rental properties remain in demand, rents are increasing, worsening affordability for low-moderate income earners.

Growing debt levels mean that many households are vulnerable to economic change. The IMF and the OECD warn that the high price of housing poses risks to the stability of the Australian economy.15 Housing debt has climbed steadily over the past decade and the housing debt-servicing ratio is worse than it was in 1989.14 Mortgage default rates are also at record levels. In the year to March 2006, court figures show that 4,873 homes were repossessed by lenders in NSW – more than 13 a day and twice as many three years ago.15

Put simply, the capacity to pay for housing has diminished over the longer term and shows no sign of abating. Affordability is not only a social problem; it is an economic problem. Key workers – vital to a diverse and competitive economy – are already being priced out of the housing market. This includes hospitality workers, transport operators, sales assistants, hospital workers, cleaners and carers.16 This spatial mismatch of housing and employment may diminish the economic competitiveness of Sydney.17

The Property Council of Australia champions more affordable housing because:

- it is essential for a vibrant, competitive, productive and diverse economy,
- it helps maintain and attract key workers, and
- it is vital in alleviating social problems.

Existing policy approaches to improve affordability have failed. Assistance is largely provided through the Commonwealth-State Housing Agreement (CSHA) which mostly funds maintaining and upgrading existing public housing stock and Commonwealth Rent Assistance (CRA) for Centrelink clients in the private rental market. Some state and local governments have attempted to use the planning system to improve affordability. Through inclusionary zoning, developers have been forced to provide affordable housing. This approach has failed to significantly boost supply, acts as a disincentive for new housing where it is enforced and is often legally contested. A voluntary and cooperative approach between industry and government would yield greater outcomes.

Land rationing, the failure to plan strategically and spatially, cumbersome and costly planning processes, and the imposition of taxes and levies, have all contributed substantially to housing being less affordable.
recommendation 1: increase land supply

Supply of land is the key factor in providing affordable housing. Restrictive and slow land release policies have contributed to increasing house and land prices. As a proportion of the average house and land package, the land component has increased from 33 per cent in 1973 to 78 per cent in 2003.22 Put simply, Sydney is now in the midst of a supply crisis. Last year only 2,500 greenfield housing lots were provided to the market compared to underlying greenfields demand of 8,000 lots per annum.22

The creation of the Growth Centres Commission and the recent audit of current and future land supply are very positive steps. But more needs to be done to secure a sustainable long term land supply pipeline. The NSW Government says that 26,000 greenfield lots are zoned and serviced. However, much of this has only occurred in the last year and it will therefore still take 2-4 years of subsequent approvals and site works before housing is available to buyers.

These challenges require a range of solutions.

recommendation 2: invest in strategic planning

Housing, jobs and infrastructure need to be co-ordinated to ensure housing is affordable. Planning decisions are inevitably economic ones as they influence the market and hence have a cost impact.

Some 60-70 per cent of Sydney’s new housing will be in established areas. Around 20 per cent of Sydney’s existing infill housing supply comes from redundant industrial lands, yet there is only 5-7 years supply of such land remaining. We need to replace 20 per cent of our infill housing supply within seven years if we are to avert a further housing supply crisis.

Significant reforms need to take place to facilitate urban renewal, reform planning instruments and improve development assessment.

recommendation 3: lower taxes & development charges

Taxes levied on property are a major constraint on affordability.

Taxes on property represent the largest area of state government revenue and account for $25 billion of taxation revenue across Australia.23 Government charges are now the second largest component of the cost of new housing, even higher than the land price.24 Government taxes, levies and compliance costs now make up 35 per cent of the cost of homes in Sydney’s north-west and 28 per cent of the cost of new units.25

Much of this goes towards infrastructure funding, but there is a greater capacity for government borrowing to fund infrastructure.

Further, maintaining the existing Capital Gains Tax (CGT) and negative gearing regime will ensure that the costs of housing in the private rental market are kept at affordable levels.

recommendation 4: boost savings

Supply measures can improve affordability, but must be coupled with a suite of demand side reforms. Demand measures can boost savings and bridge the deposit gap necessary for many to enter the home ownership market.

Measures that can boost savings in order to fund home ownership are vital in attracting and keeping key workers in cities like London and New York, and they are also valuable in helping public housing tenants break out of government dependency.

There is capacity for greater innovation on the demand side through equity partnerships, flexible loan arrangements and targeted measures to attract key workers in areas necessary to maintain economic growth.

Property taxes must be reduced.

Governments should fund infrastructure through debt, not new infrastructure levies.

Stamp duties are a barrier to home ownership and should be phased out.

Affordable housing projects should be land tax exempt.

Retain CGT and negative gearing to keep housing affordable, and provide incentives for investment in the rental market.
Addressing these fundamental supply, planning, taxation, demand and governance problems will still leave many hundreds of thousands of Australians struggling to afford rental accommodation or home ownership. It is estimated there are over one million households who are not eligible for public housing, but can’t afford home ownership. Many are the working poor and key workers vital to a competitive and dynamic city like Sydney. These people require a leg up, yet the quantum of the need is beyond government alone. In short, the private sector needs to be encouraged to invest in affordable housing.

However, private sector financing of affordable housing requires a partnership with government to be viable. Government must provide the financial framework in which private investment funds can flow into housing. The UK government has played an active role in providing these financial settings and over the past 30 years, almost A$100 billion of private investment has flowed into social and affordable housing. Similarly, in the United States there is a large and well established private investment market in affordable housing.

Engaging the private sector

Currently there is over $1 trillion invested in Australian managed funds, including superannuation funds. This is expected to more than double in the next 10-15 years when superannuation funds will hold more money than banks. It makes sense that superannuation funds should look to opportunities to invest in affordable housing through property trusts and bond schemes such as those outlined in this paper. This needs to be promoted and facilitated by government where possible. This is also a socially responsible investment, which is a growing share of the investment fund market.

### Recommendation 5: a role for the federal government

- Re-establish a federal ministry of housing, urban and regional development and prepare a national plan for affordable housing.
- Affirm a role in our cities by taking a larger role in the funding of public urban infrastructure.
- Provide low-interest loans to the states for housing projects.
- Encourage investment from the Future Fund into privately financed and managed affordable housing projects.
- Consider creating a sister Future Fund to invest in social infrastructure, including privately financed and managed affordable housing projects.
- Boost Commonwealth CSHA funding by at least 25 per cent, or $200 million, to invest in privately-developed affordable housing projects.
- Use the National Competition Policy framework to offer incentive payments to the states for housing, planning and taxation reform.
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Re-establish a federal ministry of housing, urban and regional development and prepare a national plan for affordable housing.

Affirm a role in our cities by taking a larger role in the funding of public urban infrastructure.

Provide low-interest loans to the states for housing projects.

Encourage investment from the Future Fund into privately financed and managed affordable housing projects.

Consider creating a sister Future Fund to invest in social infrastructure, including privately financed and managed affordable housing projects.

Boost Commonwealth CSHA funding by at least 25 per cent, or $200 million, to invest in privately-developed affordable housing projects.

Use the National Competition Policy framework to offer incentive payments to the states for housing, planning and taxation reform.

**FLAGSHIP SOLUTIONS**
recommendation 6: initiate a bond scheme pilot study

The Property Council supports the issuing of government bonds to the private sector to raise funds for investment in affordable housing by offering a ‘guaranteed minimum’ after tax return. Bonds can make investment in affordable housing more attractive given that it is a well understood investment class that provides a low-risk, stable return.

The Property Council presents the following bond model – developed by Jon Hall and Mike Berry with The Allen Consulting Group29 for the Affordable Housing Forum – as a joint federal and state government initiative which would provide a large-scale solution to the affordable housing crisis. It has been modelled in detail and has a number of different variations.

Key principles of the model:
- State governments issue inflation-indexed bonds that raise funds, which are used by state housing authorities or community housing providers to develop affordable rental housing.
- These bonds are guaranteed by the Commonwealth Government, with the financial risk ultimately residing with the states due to bilateral agreements. The Commonwealth underwrites the scheme and provides an additional subsidy, matched by state governments.
- Eligibility for housing under the scheme would be restricted to those on the lowest 40 per cent of incomes.
- Bond coupon payments to investors are generated by net rental returns and recurrent government subsidies, through a direct outlay.
- Principal repayments are provided from realisation of the assets at the end of the transaction, say 25 years.
- State governments implement the scheme. Taxation arrangements remain the same as for the private sector.

This model scores highly on efficiency, equity and effectiveness. An analysis by Allen Consulting suggests an initial cost to governments of $100 million per annum, growing by $100 million per annum to $1 billion per annum in the 10th year and stabilising at that level. This would need to be a nine government solution.

It is estimated that it would assist over 150,000 households annually at its peak, providing $6,560 to each household per annum. It is proposed that this model be further developed under the CSHT with all governments as stakeholders and a smaller, less costly, pilot study be carried out.

recommendation 7: initiate a securitised housing trust pilot scheme

This proposed Securitised Housing Trust would finance affordable housing while providing low income earners with a growing equity stake in their own home. This model can translate a $30 million dollar annual public contribution into an $840 million pool of affordable housing assets. It could produce 800 homes in Sydney, 900 homes in Melbourne and 1,400 homes in Brisbane.

The Securitised Housing Trust is a listed property trust which would fund housing for qualifying low and middle income earners. They would pay rent which would be distributed to the unit holders of the trust. Capital appreciation would be shared by the trust’s unit holders and the tenants, who would build an equity share in their home. If a tenant leaves the scheme, their equity can be paid out or transferred to a similar scheme.

The difference between the rental contribution likely to be afforded by tenants and the yield required by the market is around 3.5 per cent. Hence, the model proposes that governments top up the rental payments with a weekly subsidy to the trust.

Based on a 2002 cost estimate, it is expected that a Sydney-based single-income family, after meeting other costs, could afford around $200 per week in rent, representing around 3 per cent of the asset value of the home. This rent paying capacity of the occupant would need to be subsidised by around $240 per week in order to attract a rate of return sufficient to attract institutional investors.

In short, the model:
- delivers accommodation to tenants at affordable rates;
- provides returns that will attract significant private sector investment, particularly from institutional investors;
- uses government funds more effectively, rather than putting money into public housing maintenance and construction;
- gives tenants equity in their homes rather than paying dead rent money;
- removes the distinction between lower quality housing for the poor and better quality premises for the rest in society;
- supports households that are at the financially difficult stage of juggling the expense of a young family with the desire for home ownership; and
- reduces the massive maintenance costs associated with affordable housing by giving people a reason to look after premises they can one day own.

The model proposes the following annual distribution of returns:

Income: 100 per cent of income from rent distributed to unit holders.

Capital: 70 per cent of annual capital appreciation distributed to unit holders and 30 percent of annual capital appreciation distributed to the occupant.

Assuming modest levels of gearing, the result is:

Investors: A total return of 9.7 per cent per annum, which is competitive.

Occupants: An annual share of capital growth ranging from $1,800 pa in Brisbane to $3,150 pa in Sydney which can be directed towards purchasing the home they live in.

The Securitised Housing Trust creates three big winners:
- government, who are able to increase housing stock without the expensive capital and maintenance costs of public housing;
- the community, as low and middle income earners are able to realise their property ownership aspirations; and
- the private sector, who can earn stable and attractive returns on their investment.
recommendation 8: increase the role of the community housing sector and private enterprise

Finally, governments should transfer all public housing stock to the private sector for redevelopment, management and ownership. A Public Private Partnership model similar to the Bonnyrigg PPP announced earlier this year could be the template. This would enable more efficient and effective redevelopment of run-down housing stock, finance new stock through capitalisation and result in more public housing units for those most in need.

Governments should actively invest in upskilling the community housing sector and use capital grants, equity partnerships and the Future Fund to help leverage greater institutional funds into affordable housing projects, which will strengthen the capacity and effectiveness of the community housing sector.

Endnotes
