



# 7th National Housing Conference

30 October to 2 November 2012

Brisbane Convention and Exhibition Centre

People — Place — Productivity



# Australian Housing Supply Bonds



*from concept to  
implementation*

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**International Experts:** Wolfgang Amann, IIBW, Vienna and Astrid Kratschmann, Erste Bank, Vienna

**Industry Partners:** Neil Youren & Carrie Hamilton, Affordable Housing Solutions

**October 30-November 2, 2012**

**National Housing Conference, Brisbane**

# Building on extensive *research and consultation*

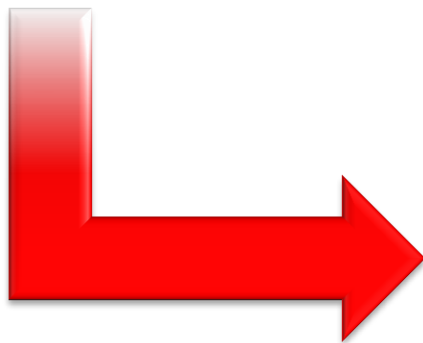
- 13 country review policy issues & innovations (AHURI, 2007)
- Comparison of alternative bond models and launch of Housing Supply Bond concept for Australia (APNHR, 2008, Housing Finance International, 2009)
- Evaluation of 6 international financial intermediaries and investment instruments for affordable rental (WA, AHURI, 2010)
- Detailed investigation of Austrian HCCB bonds and England's THFC financial intermediary (WA, AHURI, 2010)
- Extensive Australian consultation developing Housing Supply Bonds and implementation strategy suitable for Australian conditions (AHURI, 2012)

# Investigate, consult, adapt..

The development of a special purpose financial instrument for the supply of affordable rental housing in Australia.

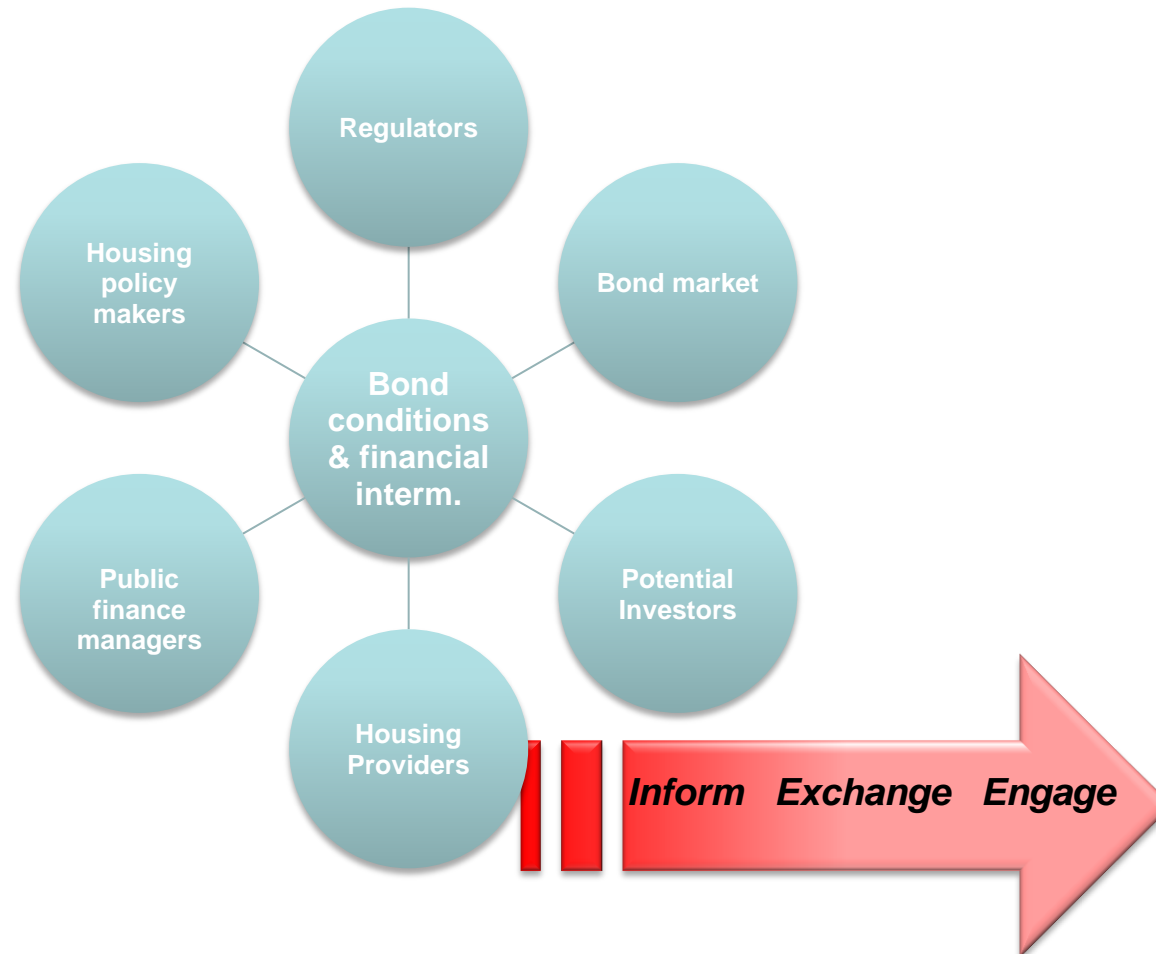


## Key questions



1. What would be appropriate **terms and conditions** for an Australian **Housing Supply Bond**, to ensure that it is attractive to investors and raises sufficient low cost funds for borrowers?
2. What **type of financial intermediary** would sell the bonds and how would funds raised be made available for approved projects?
3. What type of institutional conditions and **regulatory arrangements** would ensure funds raised are channeled to the intended purposes?
4. What **other actions** would be required to ensure success of this mechanism?

# Research process



<sup>a</sup> IIBW, Vienna and Eerste Housing Bank, Austria

<sup>b</sup> Affordable Housing Solutions, Australia (AHS)

Focused literature review  
25 stakeholder interviews, across three states

3 intensive industry meetings facilitated by research team b/n international experts <sup>a</sup> & industry partner <sup>b</sup>

Focused workshop, 18 stakeholders, research team, partner and experts

Additional public seminar, over 85 attendees

Senior policy maker consultation

# Findings – financial regulators

## **Australian Prudential Regulatory Authority (APRA)**

## **Australian Securities & Investment Commission (ASIC)**

- Australia's policy is to grow small retail bond market via standardisation, regulatory exemptions & recent tax incentives (Treasury/Finance/ASIC reforms)
- Need for quality assets & capital adequacy via regulation of banks & managed funds
- Financial intermediary and SPV could pool demands, issue housing bonds, receive payments, trustee holds assets
- CHO's need well documented revenue flows, stronger financial governance



# Findings – the bond market

## **Financial Services Council, FIIG Securities Ltd, Monash Capital Group, Frontier Asset Consultants**

- HSB a welcome concept & potential path breaker in social investment field
- Retail investors limited choices, portfolios dominated by equities
- Strong demand from fund managers for highly rated bonds – amidst drive for quality under Basel III
- FI establishes SPV to pool lending demands & issue bonds to scale, administers securitization
- Need a competitive spread above BBSW & UBS indices, lower risk/lower return thus lower cost funds
- Enhancements required such as a guarantee, purchase of junior bonds or tax incentive to improve risk-yield ratios
- These enhancements must respond to different investor segments

# Findings – (potential) bond investors

**ME Bank, Australian Super, CBUS, Financial Services Council, Australian Financial Markets Association**

- Again, HSB a welcome initiative, logical pilot for social bonds
- Wholesale market easier, requiring two steps – introduction & marketing
- Engage fund managers & asset consultants in design
- Use government, fifth column banks or not-for-profit financial intermediary as pilot, then open for competition
- Requires long term government commitment: co-financing & guarantee



# Findings – affordable housing providers

## **Community Housing Federations Australia & Victoria Large Housing Provider and Legal Advisor to sector**

- Current lending limited & costly
- Revenue curtailed by rent caps, low level of rent assistance & increasing reliance on private debt
- Supply targets not achievable under current settings
- Definition of charitable organisations narrow, affecting tax status – reforms must support broader role
- HSB a welcome concept, but requires explicit ongoing government commitment, potential in new NAHA
- Need an appropriate industry partner to perform financial intermediary role & launch a pilot scheme

# Findings – public finance

## Federal Treasury, Reserve Bank of Australia

- Direct expenditure most transparent, needs to be compared with any other strategies (tax incentive, guarantee), interest in learning about different guarantee models (WSW, BIC, THFC)
- Policy drive to expand corporate bond market & increase retail access (Finance, Treasury, ASX, ASIC)
- Recent history of government guaranteeing RMBS & partial tax exemption of bond coupon returns
- Treasury can conduct CBA of different strategies on request from responsible govt. depts.

# Findings – housing policy makers

- Recognition that current funding & policy settings not sufficient to grow affordable housing
- However, conditions for obtaining additional funding constrained; also guarantees challenging
- Implementation difficulties faced with portfolio fragmentation & NRAS need to be overcome
- National regulation needs to meet investor expectations
- Austrian model has direct applicability – federated system, legislatively based, links to planning & land supply policy
- Several states showing strong interest in financial innovation for housing / social investment purposes

# Review of findings against research questions

<i>Terms and conditions of HSB?</i>	<ul style="list-style-type: none"> <li>✓ A straight forward, low risk, low yield and long term instrument required to provide cheapest funds</li> <li>✓ Enhancement required to reduce risk and enhance low yield</li> <li>✓ Tax incentives need to be devised so they are equally valuable to those with high and low tax rates</li> <li>✓ Guarantees are very interesting for low risk long term investors - insurance funds, certain portfolios of super funds, banks, retail investors</li> </ul>
<i>Financial intermediary?</i>	<ul style="list-style-type: none"> <li>✓ To pool funds for scale</li> <li>✓ Specialist knowledge of sector</li> <li>✓ SPV to issue bonds, linked to CHO loan obligations</li> <li>✓ Optional forms : Public, Not-for-profit, For profit</li> </ul>
<i>Regulatory requirements?</i>	<ul style="list-style-type: none"> <li>✓ Beyond benchmarks, ensure sector regulation meets investor standards</li> <li>✓ Strengthen financial capacity of providers and reduce risks to lenders</li> <li>✓ Use to promote innovation and solutions rather than impede growth</li> </ul>
<i>Related requirements?</i>	<ul style="list-style-type: none"> <li>✓ Capacity to repay based on revenue stream</li> <li>✓ Rent assistance and eligibility policy critical</li> <li>✓ Long term and consistent policy vision by governments</li> <li>✓ Facilitative planning and land supply to reduce development risk</li> </ul>

# Recommendation 1

## An appropriate Financial Intermediary

*This would:*

- Link suppliers of capital with appropriate investment opportunities
- Create aggregation benefits & efficiencies, through lower transaction & search costs
- Develop further efficiencies through specialised knowledge of the industry
- Ensure a pipeline of projects & funds
- inform and educate investors & providers about risk / returns

*The intermediary could also:*

- Assist in making providers investment ready
- Provide access to funds for smaller players – helps maintain diversity
- Contribute stability to housing & finance systems via counter cyclical activity

*Form:*

- A not-for-profit specialist intermediary is likely to be more cost effective
- Newly formed or build on established agency?

# Recommendation 2

## Marketable terms & conditions

The specialist intermediary would issue a suite of Housing Supply Bonds  
Each tranche would have different risk and return & thus initial yield  
Different enhancements would attract different potential investors

Investor segment	Bond type	Characteristics & enhancements
Super fund managers (15% tax rate)	AAA Housing Supply Bond	A fixed interest, long term (up to 10 years) AAA-rated bond – implying need for a government guarantee
Retail investors (30-48% tax rate)	Tax Smart Housing Supply Bond	A fixed term, fixed interest (or indexed) lower yield long term bond with a tax incentive to generate a competitive after-tax yield
Governments	NAHA Growth Bond	A zero interest bond that converts a direct grant into a long term revolving loan

# Recommendation 3

## Cost reducing enhancements

Under current settings finance is too costly – constraining supply outputs & affordability

Three enhancements are proposed to reduce the cost of funds

1. Government support through the NAHA Growth Fund – via **subordinated long term zero interest loans** – to provide collateral to underpin bond issues
2. Additional support to fund a contingent liability **fund covering the guarantees** on AAA Housing Supply Bonds
3. **Tax concessions** to investors in Tax Smart Housing Supply Bonds

Additionally, CRA (for low income tenants) and NRAS (for investors) continue in current/reformed forms to assist affordability outcomes

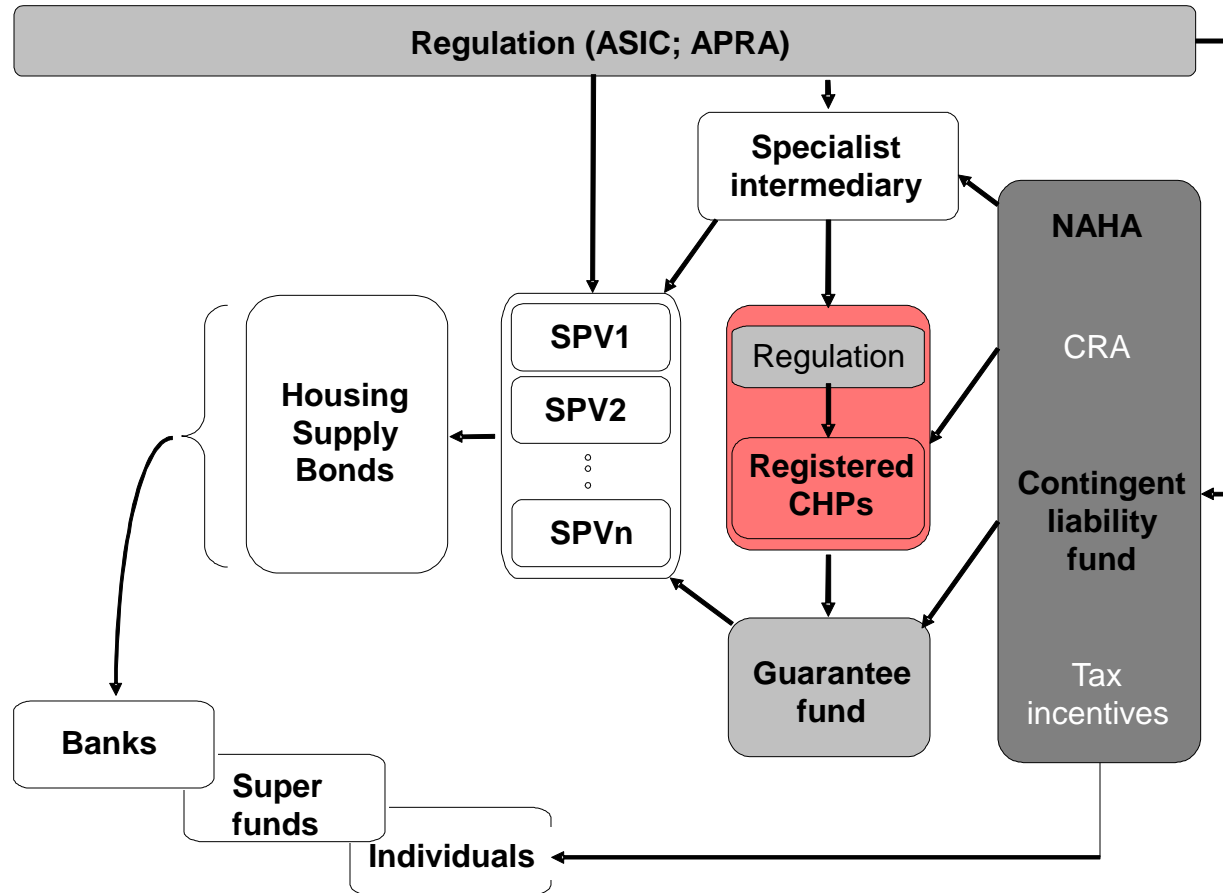


# Recommendation 4

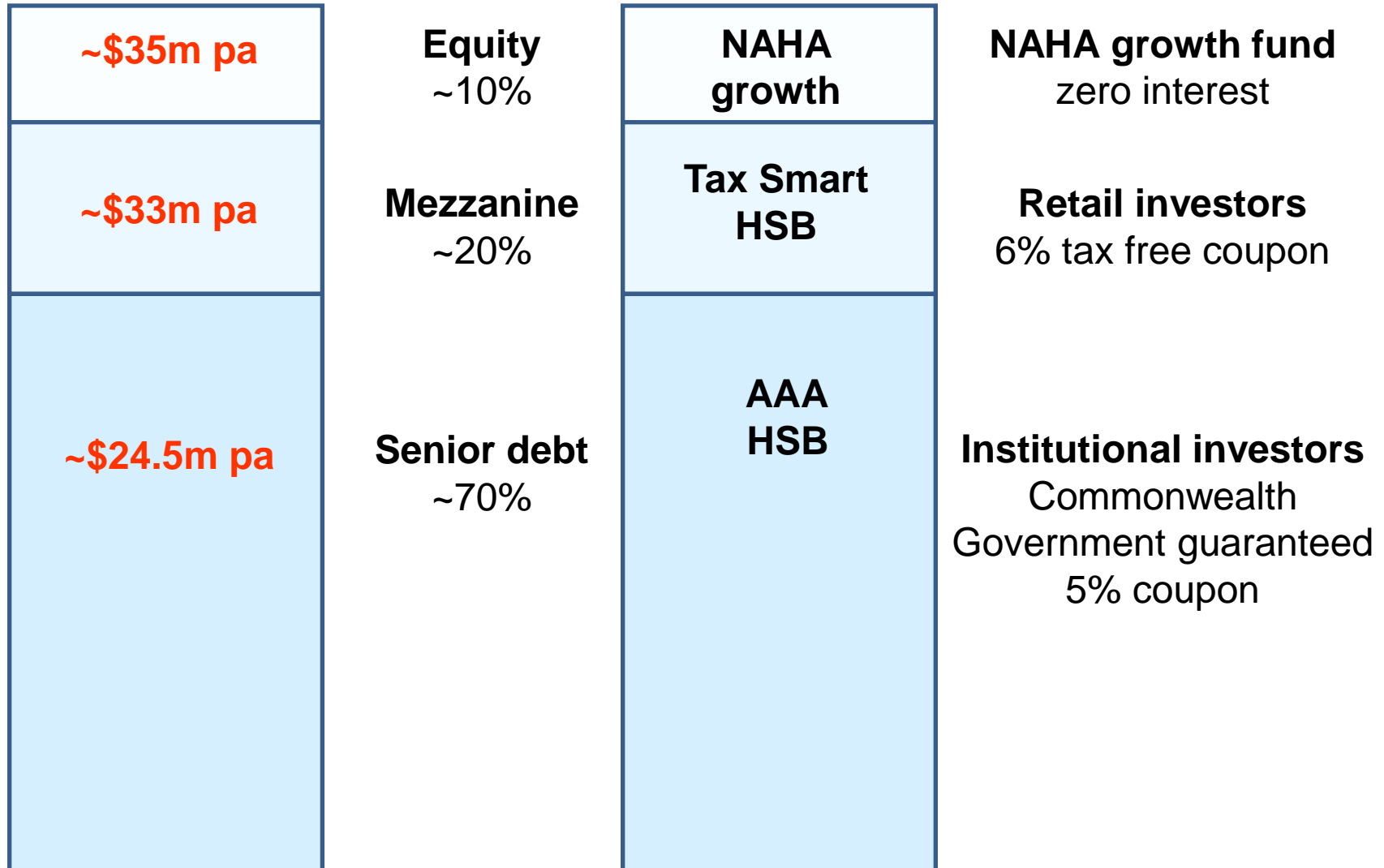
## Regulate to reduce risks

- Financial auditing – eligibility for funding & tax privilege
- Performance reporting – with appropriate sanctions
- Adherence to legislated business model & social policy targets
- Competitive application for loans & grants
- Transparent decision making on outcomes
- Drive cross-sector development, solidarity & innovation

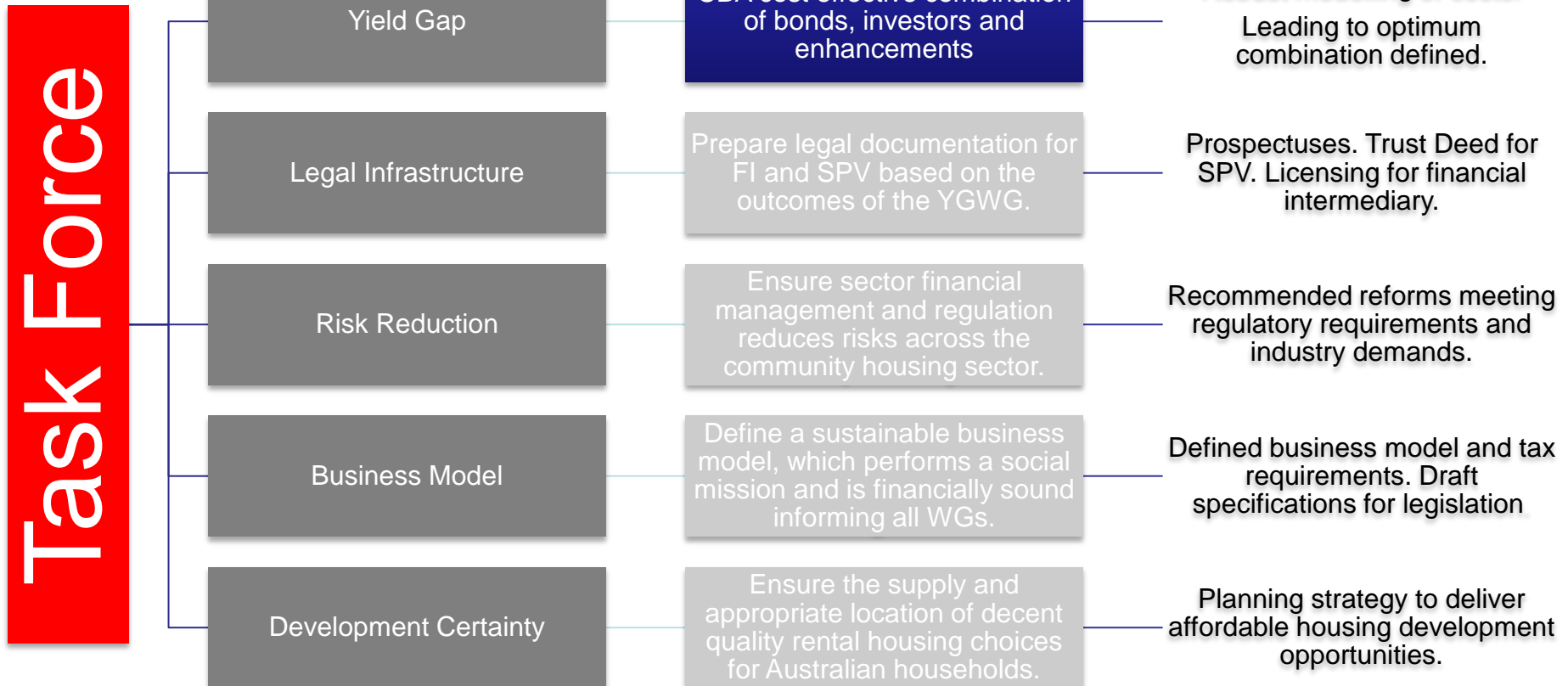
# Proposed architecture



# Indicative annual cost to raise \$7b (per 20,000 dwellings pa)



# Strategy for implementation – task orientated expert working groups



# Progress since release of research..

- *May 2012 Final Report released*
- *Extensive media coverage (Financial Review, The Age, ABC Radio, Housing Finance International)*
- *Broad discussion at professional, industry, research, policy (NAHA) forums and recently at C/wealth ministerial level (with key financial stakeholders)*
- *Active consideration of bonds by several states*
- *Awaiting C'wealth response, NAHA commitment*
- *Residential construction hits record lows, CH pipelines dry up*
- *Stimulous II developments progress (UK housng bonds guarantee)*

*Onwards!*

# Further information



Read the published reports, presentations, articles and media coverage on this project at:

<http://www.ahuri.edu.au/publications/p30652/>

Or contact:

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**Thank you.**