Housing Legislative Package – Housing Australia Future Fund Bill, National Housing Supply and Affordability Council Bill and Amendment Bill

January 2023

HESTA welcomes the opportunity to make a submission on key elements of the Government's housing legislative package. This package of legislation represents a significant undertaking from Government to partner with institutional investors on financing models that create the conditions investors need to scale their investment in affordable and social housing. Our submission focuses on areas of the package that we believe will enhance its ability to facilitate institutional investment at scale.

HESTA and our members

HESTA invests around $70 billion of assets on behalf of more than 970,000 members who work in caring industries, primarily in the health and community services sectors. Almost eighty per cent of our members are women and most are on low-to-middle incomes. Our members are key contribution workers who deliver critical, life-changing services, and whose work generally requires their physical presence. They are increasingly struggling to afford housing near where they work, and housing costs are a key factor determining their financial security in retirement.

Australia's housing crisis presents risks and opportunities for investors. While housing shortages reduce productivity across the economy, they also provide the opportunity for investment innovation to deliver our members appropriate risk adjusted investment returns by improving housing supply. This innovation requires investors to work with governments on policy settings and financing models that will allow institutional investors to scale their investment in social and affordable housing. HESTA is pleased to support the Government's Housing Accord to progress this important work.

As home ownership has become less attainable for low-to-middle income earners, rental affordability has dramatically decreased, and rental vacancies have dropped to long-term lows nationally. HESTA's focus is on improving the supply of housing that addresses this gap by increasing the availability of well-located social, affordable and market rate rental housing that meets the needs of low-to-middle income earners like our members. HESTA supports the Government's acknowledgement of the need to address this housing gap for frontline workers.

The need to scale institutional investment

A significant allocation of private capital is required to address Australia's chronic undersupply of social and affordable housing. This undersupply has been driven by underinvestment by governments, alongside a range of barriers to institutional investment that has meant that institutional investment in new rental housing has tended toward the high end of the market.

For many years, super funds, including HESTA, have considered and delivered investments in affordable housing that work within specific parameters for certain developments, but there have been barriers to scaling these approaches to the extent needed to deliver sufficient housing supply. There is a need for innovative financing models that facilitate the allocation of capital to pipelines of projects at scale, and provide diverse ways for institutional investors to access investment in the sector.

HESTA supports the prudent use of public capital to catalyse new markets for investment and we welcome the Government's commitment to provide a funding stream through the Housing Australia Future Fund that addresses the financing gap for investment in social and affordable housing, and to work with investors on financing approaches that will maximise the allocation of much-needed capital in this emerging sector.

Build-to-rent: HESTA and Super Housing Partnerships

Developing the build-to-rent sector into an institutional asset class will be key to meeting the housing needs of low-to-middle income earners. Compared to other jurisdictions like the US, where build-to-rent makes up a higher portion of institutional property portfolios, Australia's institutional build-to-rent sector is in a fledgling state, with a lack of institutional product. Build-to-rent developments are held by institutional investors over the long-term, delivering an overall increase to housing supply and providing stable housing choices to working Australians.

To start addressing this challenge, HESTA, as a founding investment partner, is expecting to commit $240 million towards developing mixed-tenure, built-to-rent apartment projects alongside new specialist affordable housing investment manager, Super Housing Partnerships. Super Housing Partnerships has the capability to aggregate institutional capital for delivery of a pipeline of affordable housing developments in partnership with community housing providers and specialist developers. Providing institutional investors access to a platform for scalable investment in residential projects with a focus on social and affordable housing is a first in Australia.

HESTA's investment is earmarked for mixed-tenure developments that include social, affordable and disability accommodation alongside market rate dwellings. This mix has advantages for tenants and investors. Market-rate dwellings cross-subsidise affordable dwellings, and social outcomes are furthered where dwelling types are mixed on a tenure-blind basis. For investors, the tenure mix provides a smooth income profile with stable rental income, low vacancy rates and high demand that is less exposed to economic downturns. Effective financing models would maximise the balance of discounted housing that can be provided in these developments.

Creating conditions for scaling investment

Consistency through outcomes-based definitions

To support innovation in how social and affordable housing is delivered, while ensuring Government support is well targeted, there is a need for an agreed, consistent approach to defining both affordability, and the parameters that should apply to qualifying social/affordable housing projects. Defining qualifying developments at project level supports achieving scale. Outcome-based definitions guide targeted provision of public support and are a critical element in leveraging private capital to deliver social outcomes.

Qualifying projects should include a minimum quota of social/affordable housing (40% would provide a meaningful contribution), based on an agreed definition of affordable housing, to determine the level of Government support. HESTA proposes a definition of affordability based on real incomes for workers like our members. This would set rents to deliver housing at no more than 30% of household income.

> *Recommendation 1: Set parameters for qualifying affordable/social housing projects, and agree a definition of affordability based on real incomes*

Financing models should facilitate both debt and equity investment

For a number of years, National Housing Finance and Investment Corporation (NHFIC) has provided the capability for institutional investors to provide debt financing to community housing providers through their bond aggregator. HESTA holds NHFIC bonds, and we have found these government-guaranteed securities to have defensive and diversifying characteristics that are attractive for inclusion in our broader portfolio. However, this approach is not sufficient to support the scale of investment needed to deliver the required housing supply. We welcome the opportunity the Housing Australia Future Fund presents to develop new approaches to financing.

There is an opportunity to develop financing models that facilitate the scaling of equity exposure to affordable residential property assets. Equity investment will accelerate the development of the build-to-rent sector into an institutional asset class, and maximising the level of social and affordable housing that can be provided in these assets is an efficient way to increase the provision of social and affordable housing.

Financing models should support innovation, allowing for new approaches, including the development of investment vehicles that give institutional investors equity exposure. To allow this innovation while ensuring housing needs are met, it is crucial that government support is targeted and outcome based. To support this, provision of financing under *Treasury Laws Amendment (Housing Measures No. 1) Bill* should be contingent on the housing outcomes delivered, while allowing for innovation in investment vehicles and ownership structures.

> *Recommendation 2: Financing models should facilitate scaling of institutional capital through both debt and equity investment*
>
> *Recommendation 3: Financing models should be outcomes focussed, taking into account the need for innovation in investment vehicles and ownership structures*

Financing models should deliver certainty and transparency

To ensure that financing models raise sufficient capital, they must provide investors with the stability and transparency they need to ensure that risk is accurately priced. Superannuation funds favour long investment timeframes, particularly with regards to unlisted assets such as residential property. Unlisted assets are well suited to patient super fund capital, delivering value for members over the long-term.

Stability can be provided by reducing the possibility of political or regulatory change and intervention to enhance funding certainty. This is supported by:

- Long-term decisions by policy-makers that increase certainty for investors
- Ensuring funding available to meet obligations to investors is as predictable as possible

There are concerns that some of the provisions in the *Housing Australia Future Fund Bill* don’t deliver the certainty required to maximise the provision of capital. The Bill relies on annual Government decision-making processes that increase the level of uncertainty. The Bill is also unclear how much of the funding will be available to support investment through NHFIC and how much will be available for other purposes. These uncertainties may result in a higher expected level of return to compensate for the potential higher variability in investment outcomes.

In addition, the development of debt financing models should ensure investors have access to transparent data to allow them to assess and price risk accurately. Notwithstanding government support, reducing uncertainties and provision of relevant data to investors will facilitate investors’ robust evaluation of underlying project risks and exposures for any future debt financing opportunities.

Recommendation 4: Financing models should be structured to minimise uncertainty and deliver a predictable flow of funding

Recommendation 5: Reporting should include the data that investors require to accurately assess and price risk