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Submission to the Productivity Commission Inquiry into First Home Ownership

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The Tenants Union of Victoria

The Tenants Union of Victoria Ltd (TUV) welcomes the opportunity to contribute to the Commonwealth Inquiry into First Home Ownership. The TUV is a specialist statewide advocacy organisation and community legal centre, established in 1975, that provides free information and advice to residential tenants, rooming house and caravan park residents across Victoria. In the year 2001/2002 the TUV assisted almost 34,000 private and public tenants and residents in Victoria.

The vision of the TUV is for genuine housing choice without social or economic disadvantage. Our mission is to promote and protect the rights and interests of all residential tenants in Victoria.

The TUV also promotes community awareness of tenancy laws and issues, lobbies for tenancy law reform and provides accredited training on a statewide basis for tenant and housing workers. The TUV produces a number of publications throughout the year including multilingual information in 11 community languages, a journal on tenancy issues entitled 'Tenancy Quarterly' and a broadsheet publication for tenants entitled 'Tenant News'. In previous years the TUV has been a member of a number of State Ministerial Advisory Committees related to housing and tenancy issues, and currently has a seat on the Victorian Ministerial Housing Council.

This submission will address point F in the Terms of Reference.

The operation of the total housing market with specific reference to the availability of a range of public and private housing types, the demand for housing and the efficiency of use of the existing residential housing stock.

In particular the submission will focus on housing affordability in the private rental market as the main alternative form of housing for prospective first home buyers. We believe the growth in investment in the rental market, coupled with the lack of affordable rental properties available to low income households, is adversely impacting on the capacity of lower income households to become prospective first home buyers. This submission provides an overview of the current state of the private rental market, the recent trends in relation to investment in the market, and the role of Commonwealth Rent Assistance in ensuring genuine affordability and other housing outcomes for very low-income households. This submission argues that many low-income households are constrained by the operation of the rental market and do not have adequate exit options, either into home ownership or social housing.

There are a number of policy levers available to government that will assist in improving the housing outcomes of low-income households. These include the creation of incentives to target investment to the affordable end of the rental market, review and reform of Commonwealth Rent Assistance (CRA), and strengthening of state based tenancy laws, particularly in relation to security of tenure.

The Private Rental Market in Australia

The Australian housing market is complex and inter-related. The major tenures of home purchase/ownership, and public and private rental do not function in isolation but are inextricably linked.

The current problems of affordability for first home buyers are arguably reflected in the increase in the numbers of households living in private rental, and the length of time that they remain in this tenure. The role of the private rental market in the 'housing career' of Australians has changed considerably over the last ten to fifteen years. Following the Second World War, private rental was seen as a transitional option for households on the way to home ownership or public housing depending on their financial situation.

Households are now staying in the private rental market for longer and accessing home ownership much later, if at all. The reasons for this are many and varied and like the market itself, should not be viewed in isolation. "Affordability" is but one part of the equation. There have been a number of significant structural changes in the way Australians live. Changes to the labour market, distribution of incomes and demographics (Berry and Hall 2001, ABS 2000, DOI 2000, Cheers 1998) have resulted in an increase in sole person and sole parent households, delayed family formation, longer periods spent studying, educational debt and reduced job stability. All of these factors have influenced access to home ownership.

At the other end of the spectrum, low-income households who would have traditionally moved into public housing are finding access to this tenure restricted. Both State and Federal governments have been unable or unwilling to increase public rental housing. Static or in some instances shrinking supply of public housing has meant that access is targeted to those most disadvantaged. More than 60% of households gaining access to public housing are experiencing another form of significant social disadvantage (drug and alcohol addiction, mental illness, escaping domestic violence) on top of homelessness. In Victoria, for about 70,000 dwellings in the public housing portfolio, there are more than 40,000 households on the waiting list and in 2001/02 only 6993 new households were assisted. Public housing has moved from affordable housing to welfare housing, and is no longer an option for households' simply experiencing affordability problems in the private rental market.

The role of the private rental market within the broader housing market has taken on greater significance throughout the 1990s (Seelig 2001). The increasing demand for private rental housing has created a shortage of low cost rental properties (Wulff, Yates and Burke 2001).

In terms of the choice-constraint dichotomy, the reality is that the Australian private rental sector serves a dual function, providing choice for the more affluent and constraint for the poor (Burke 1999:11)

The private rental market is highly segmented offering choice and flexibility for some households but usually only those for whom affordability is not an issue. In Melbourne, the recent boom in inner city apartment construction has resulted in a glut of rental properties at the higher end of the rental market with little or no impact at the low cost end.

Ironically, there is evidence that some households who are in a position to exercise market choices, trade down in private rental, paying cheaper rents for less amenity and effectively squeezing out low-income households who are reliant on the private rental market for long-term housing. Significantly, low cost (ie low rent) housing in the private rental market declined by 28% between 1986 and 1996, at the same time as there was an increase in low-income households renting privately (Wulff & Yates w Burke). The result in Victoria was a shortfall of 36,000 low cost properties across both metropolitan and rural areas in 1996 (Yates).

With few options, low income and marginalised households are spending long periods of time in private rental (Wulff 1997, Beer 1999), often in housing stress (Yates and Wulff 2000). Those who find themselves unable to access the private rental market, slip into even more marginalised forms of housing such as rooming houses and caravan parks. The private rental market has failed to adapt to changing demands, and improvements need to be made across a range of areas to ensure that the needs of low income and marginalised households are met.

Little low cost private rental housing is purpose built and a mismatch between the private rental stock profile and the changing demographics drives competition for limited stock. In addition, the spatial arrangement of supply does not assist locational choice particularly movement to areas of increasing employment opportunities.

Many low-income households also trade off amenity for cheaper rent or share in overcrowded situations (Burke 1998). Data on the standard of private rental accommodation in Australia is scarce (Paris 1993), partly due to the nature of the private rental market and the exchange of properties between private rental and home ownership markets (Seelig 2001). However, many private rental dwellings lack basic features, such as heating/cooling, that are consistent with community standards of appropriateness.

Discrimination is a barrier to many households attempting to access private rental (San Pedro 2000, Adkins et al 2001). While recourse is available through Equal Opportunity legislation, the complainant must fit within a specific category and the process is often slow and does not ultimately help to secure accommodation.

Affordability is a significant issue for households in the private rental market, more so than households in any other tenure. The Affordable Housing National Research Consortium (AHNRC) found that private tenants are the group most likely to be dealing with housing affordability issues (AHNRC 2001). Their research shows that 54% of private tenant households are experiencing housing stress (paying more than 30% of their income in housing costs), which is twice as high as households who are purchasing, and six times higher than households living in public housing (AHNRC 2001). In the state capital cities of Australia, nearly 3 out of every 4 private renter households in the lowest 40% of total incomes are experiencing housing stress (Berry and Hall 2001).

Housing stress can be addressed through either supply side or demand side responses. Supply side responses consider ways in which the supply of low-cost housing can be increased, either through private or public investment in affordable housing. Demand

side responses consider the types of subsidies provided directly to households in order to improve the capacity of the households to maintain housing that is appropriate and affordable. The following submission will look at the supply side issues of investment in private rental and social housing and the demand side of Commonwealth Rent Assistance. It will also consider measures to increase standards in rental housing so that some of the societal benefits of homeownership can be transferred to the private rental market.

Investment in the Private Rental Market

Investors in housing have increased in actual numbers and in percentage of total housing loans over the past 10 years. In June 1993 only 23% of the total monthly amount loaned for housing went to investors, by June 2003 this had increased to 40%. This equates to a dollar increase from \$1,028,000,000 to \$6,880,000,000. The actual monthly amount increased 6 fold in 10 years, while the amount lent for owner occupied properties had only a 3 fold increase in the same period (ABS 2003).

The increase seems to be most pronounced in the past few years. In just 2 years lending for the purpose of buying rental properties almost doubled from a total of just over \$30 billion in 2000 to more than \$57 billion in 2002. This compares to an increase of less than 30% in lending to owner occupiers (ABS 2003). The Real Estate Institute of Australia (REIA) Residential Investment Property Index shows strong property market growth on annual returns, with Melbourne leading the way with average annual returns of 16.5% over the past decade (REIA 2003).

There is little recent data on what these investors look like however. The most recent ABS investor profiles are from 1999 drawing on 1997 data, prior to the real boom in investing. In 1997 just over 76% of investors owned or part owned only one rental property. Householders (as opposed to businesses and non-profit institutions) provided approximately half the rental housing for the private market. Colloquially termed “mum & dad” investors, most already own their own home, with almost half owning it outright.

The majority of these investors are couples of working age, with 59% aged between 35-54 years. Couples were 3 times as likely as singles to own an investment property. We can assume this is attributable to higher earning capacity. Median gross weekly income of investor units in 1997 was more than double the median of all income units.

Of current investors in 1997, 66% cited desire for a long-term investment as their main reason for investing, with only 16% attributing their reason to negative gearing. Intending investors were slightly higher with 80% and 23% respectively. Existing investors were also more likely to site “possible future home” and rental income than intending investors (ABS 1999).

There was no major shift in the make up of investors from 1993 to 1997 (ABS 1995). More research is needed to see if this investor profile is still applicable in 2003. Certainly the numbers of investors have increased due to a combination of factors including low interest rates, poorly performing superannuation, collapse of the share market and income tax levels. This has been further exacerbated by financial

deregulation in the 1980s that, when combined with low inflation, has led to greater availability of finance.

There is obviously a correlation between increase in investors and increase in rental accommodation. The media has been frequently reporting on the “renter’s market” with stories of vacancy rates and tenants negotiating for better deals. However as already stated, the rental market is highly segmented. Investors are investing in housing that they believe will provide good capital gain and “quality” tenants. Tenant stereotyping has become ingrained and there is a belief that the more expensive the rent the better the tenant will be. The result is an increase in rental housing at the medium to higher end of the market. Theoretically if the market is working effectively this would provide a filter up approach, with those on higher incomes being attracted into higher end rentals thus freeing up some of the rentals at the lower end of the market. To date however, this has not occurred.

The reason for this can be found by examining why higher income households are trading down. Anecdotal evidence suggests that households trade down in order to save to buy a house. Higher income households trade off amenity because they see private rental as a temporary situation. As housing prices increase people stay in the private rental market for longer while they save for a deposit.

What is needed is an incentive to encourage investment in low rent properties. Low rent properties are not necessarily low cost properties. For example in the inner city where the property boom is driven by land costs, the actually dwelling may add little value to the property and may not attract high rents. If the main objective of investors in housing is long term capital gain and not income then there should be opportunities, with the right incentives to channel investors into low rent stock.

Recommendations

- 1. That incentives are developed that encourage long term investors to invest in low cost rental housing***
- 2. That mechanisms are developed to ensure that low income households are matched with low rent housing***

Private Rental Affordability – The Role of Commonwealth Rent Assistance

This section will argue that affordability remains a significant problem for many low-income households living in the private rental market despite the investment of significant funds through Commonwealth Rent Assistance (CRA), and that an independent investigation of the effectiveness of CRA is needed to address this problem.

Any discussion on reform of CRA inevitably leads to discussion on the impact of changes to CRA on rent setting. There is however, no empirical evidence that confirms that CRA is rent inflationary. Research conducted by Econsult (1991:29) showed that real estate agents set rents in relation to market forces, and although some community agencies strongly argued to the contrary throughout the 1970’s this view has not continued through the last decade (Johnston 2002).

Cost to Government

In 2001/02 the Commonwealth government spent \$1.8 billion on CRA. Expenditure on CRA currently exceeds the Commonwealth and State contributions to the public housing system through the Commonwealth State Housing Agreement (CSHA), which for 2000/01 was \$1.4 billion. CRA is paid to households in receipt of a Centrelink income, and is paid at 75 cents for every \$1 above the minimum rent (currently \$82.80) to a ceiling of \$207.07 (Centrelink 2003:24). However there is reason to believe that CRA is not assisting low-income households to achieve affordable and appropriate housing outcomes in the private rental market, that allow households to exercise genuine housing and lifestyle choices.

Affordability Measurement

In determining the effectiveness of CRA in relation to affordability, consideration needs to be given to how housing affordability is measured. Burke (2002) has identified two distinct methods for calculating housing affordability. The housing first model assumes that housing costs, or rents, will be prioritised in the household budget, with all other expenses paid after this. Burke refers to this as the 'housing first model' (2002:6). This model is based on a historical concept developed by commercial lenders in assessing the risk of lending to households. It is the measure that was adopted by the National Housing Strategy (NHS) and is used by both state housing authorities in setting rents, and Department of Family and Community Services (DFaCS) when assessing the affordability outcomes of CRA.

The second model, the housing residual model (Burke 2002:6), gives priority to non-shelter necessary expenses first, with the amount remaining determined as the amount the household can afford. The benefit of the housing residual model is that it accounts for differences in household size and expenses. It is a needs based approach to housing affordability, rather than housing first, which as a one size fits all approach does not provide flexibility or take into account the differing priorities of large families or households with medical or other significant expenses.

In 1991 the NHS identified housing affordability as rent of no more than 25% of household income, a figure that has been generally accepted as an appropriate housing affordability benchmark. 30% has been used to highlight households experiencing housing stress.

CRA Financial Outcomes

DFaCS uses the 30% of income as rent to measure the success of CRA (DFaCS 2002:111). Indeed a further measure of the effectiveness of CRA by DfaCS is to show the numbers of households who pay more than 50% of their income in rent before and after receipt of CRA, double the informally accepted benchmark of housing affordability (DFaCS 2002:111).

Current reporting of DfaCS on the performance of CRA shows that after CRA is paid 33% of households or 322,190 households, are paying more than 30% of their income in rent (DFaCS 2002:11). CRA reporting however, does not address how the benchmark of 30% was reached as an appropriate measure, nor is there consideration given to the possibility that 30% as a measure is too high. It is very likely that many extra households would be evident in the 25-30% range and that this reporting approach grossly underestimates the level of housing stress after CRA.

The measurement of housing affordability is now a contested area that is ultimately linked to the adequacy of incomes and poverty issues. Agreement needs to be reached on this important measurement, before housing affordability issues can be adequately addressed for low-income households.

Recommendation

- 3. That, in consultation with the community and housing sector, a housing affordability benchmark be developed.***
- 4. That the housing affordability benchmark be used to assess the effectiveness of CRA in relation to affordability outcomes for recipients.***

Regional Variation

The rental market is not a homogenous market, but instead is highly segmented. Access, standard of properties and rent levels vary from the high end of the market (for example >\$300 pw) to the low end of the market (<\$150 pw). Rents vary between capital cities, within capital cities and throughout regional Australia, which obviously affects the average amount of CRA paid in certain regions. There may be potential to account for regional variations by reducing the level of subsidy in low rent areas in order to finance the increases in subsidy required in high rent areas such as metropolitan cities where affordability is a significant problem. However reliance on averages can mask significant variances between the top and bottom rents in a region, and could compound affordability problems for some households living in low average rent areas but paying higher rents.

The establishment of boundaries that delineate regions will be a difficult task. The boundaries would need to be carefully selected and regularly reviewed in order to account for fluctuations in the local market. Forthcoming work by NATSEM may provide further insight and possible solutions on the issue of regional variances.

Recommendation

- 5. That, in consultation with the community and housing sector, further work be undertaken on the need for and appropriateness of regional variation of CRA payments.***

Non-financial Housing Outcomes

The Minister for Family and Community Services, at the National Housing Conference in Brisbane in 2001 stated that the advantage of CRA is that it can move to “where the jobs are” (Vanstone 2001). However if there are no affordable rental properties available in high rent areas, households will be constrained from moving to “where the jobs are”. Wulff (2000) found that CRA recipients were less satisfied with their access to work opportunities than all other private rental households, suggesting that the cost of rental has more influence on locational choice than access to job opportunities.

A further problem with the CRA program is the failure to use CRA to leverage improved non-financial housing outcomes for low-income households. The public housing system currently includes a portfolio of \$30 billion in assets, in comparison to

CRA where, despite the significant money spent, no assets are accumulated and private landlords are not required to meet any standards of amenity. This is at odds with similar programs in other countries, such as the housing voucher system in the US, which includes benchmarks for standards.

There is little quantitative research on the physical standard of properties in the private rental market (Paris 1993). Qualitative research by Wulff (2000) shows that 63% of CRA recipients consider that their dwelling is in good to very good condition. However the research does not analyse whether a “value for money” (Wulff 2000) judgement is implicit in the responses. The remaining 36% of households, or more than 300,000 households, consider their property to be average to poor. Although not the majority of households they represent a significant proportion of low-income households who are living in accommodation not suitable to their needs.

The lack of security of tenure for low-income households in the private rental market results in increased costs due to unplanned and forced relocations. Utility charges, removalist costs and dislocation from social networks, health professionals and schooling all involve immediate tangible and longer term intangible costs. There is no data available on the numbers of households who move involuntarily by tenure. Further research needs to be undertaken in this area.

Recommendation:

6. That housing outcomes be benchmarked for CRA recipients including security of tenure, affordability and standards.

A comprehensive and independent review of CRA needs to be undertaken in conjunction with the community and housing sectors. The review should address the issues of affordability, regional variation, locational choice and housing outcomes, including benchmarking of standards such as physical standard of property, security of tenure, affordability and increased payments for higher standard accommodation.

Security of Tenure

Many households living in the private rental market do not currently experience adequate security of tenure in relation to their housing. In Victoria 67% of tenant households, or 444,200 tenants, moved in the three years prior to 1999 (ABS 1999). It is not known whether these moves were forced or voluntary. It is clear however, that tenants have a significant lack of control over when they move, and the amount of time they are allocated to find alternative housing. Tenant households move far more frequently than households in any other tenure.

The lack of security of tenure dislocates people from their communities, friends and support networks, schooling and local health services.

There is evidence that permanent, secure housing provides the necessary base for ‘social capital’ (ie the mutual trust and social behaviours) that facilitates civic engagement. Neighbourhood stability, in the sense of low resident turnover, is associated with high levels of social capital and good, basic,

housing standards. Conversely, where that social capital disintegrates, so does social cohesion. (AHNRC 2001:19).

The corresponding insecurity is a powerful disincentive when tenants are considering the exercise of their tenancy rights. This is commonly manifested through a reluctance of households to pursue repairs, challenge a rent increase or question their right to privacy and quiet enjoyment of the rented premises. This can result in a household moving 'voluntarily' as they are not able to address other outstanding problems in relation to the property.

High mobility leads to high transaction costs, which significantly inhibits the capacity of renter households to save for home purchase. Transaction costs include the cost of removalists, disconnection and reconnection of utilities and other associated costs such as forwarding of mail and purchase of new school uniforms for children. A lack of control over mobility means that households are unable to plan for these expenses, and often have little time to prepare.

Improving security of tenure for households in the private rental market will enable households to save for home purchase. It will also enhance the capacity for the development of genuine social capital.

Greater security of tenure can be achieved through strengthening of state based tenancy legislation, and changes to the standard practice of real estate agents. In particular the abolition of no reason notices to vacate, and offering of long fixed term lease agreements.

Recommendation:

- 7. That state based tenancy laws be strengthened in relation to security of tenure***
- 8. That long fixed term leases be readily available in the private rental market***

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