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Submission to Senate Inquiry into the *Housing Australia Future Fund Bill 2023* and other bills

Dr Cameron K. Murray
Research Fellow, Henry Halloran Trust, The University of Sydney

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https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/HousingPackageofBills

Summary

The proposed Housing Australia Future Fund (HAFF) is a bad policy. Its main outcome is to unnecessarily pay millions each year in fees for financial management.

If the objective is to make homes cheaper for Australians, it is not clear why the HAFF is better than doing nothing.

The basic problem is that the HAFF does not produce new below-market housing of any sort. It instead uses money to buy non-housing assets.

Just like forcing households to buy non-housing assets with their income makes it harder for them to buy a home to live in, so too does the HAFF make it harder for governments to invest in housing.

The $10 billion could be spent on building or acquiring new public housing directly, or via state public housing agencies rather than on non-housing assets. If financial trickery is desired, these funds can be swapped for equity shares for accounting purposes.

What seems to be overlooked it that housing, including public housing, is a financial asset that makes a high return over time.

In fact, the total return on the typical Australian home has exceed the total return on the Future Fund, which would manage HAFF investments, since its inception in 2006. The bulk of this housing return comes from capital gains, which are returns that also accrue to public housing agencies who rent far below market prices.

This is why public housing is well known to be the most cost-efficient way to provide below-market priced housing to residents, and why instead of a HAFF these funds should be used to directly build more public housing dwellings.

Background

My understanding of the HAFF design is as follows.

- The HAFF will be $10 billion fund managed by the Future Fund board, which will trade that cash for listed financial assets.
- The HAFF will hopefully make a margin over the opportunity cost of these funds, which is the rate of interest on government bonds.
- When the HAFF makes a positive margin over its cost, these net gains can be withdrawn from the fund to use to build new homes to a maximum of $500 million per year at the Minister's discretion.
- It is not clear what happens when the HAFF makes a loss.
- It is not clear for what purpose these grants can be made.

Off balance sheet tricks

The basic idea of the HAFF is to create an off-balance sheet accounting trick whereby the debt associated with the fund, and the assets in the fund, are considered as a bundle and hence not counted in measures of public debt.

But the same trick can be done with direct investment in housing, whereby the debt and the equity can be allocated to the balance sheet of the fund that owns the houses.

There is nothing to be gained by only buying assets in a fund that are not residential property assets.

In fact, if buying high-return financial assets is the best way to fund public spending, then this is always true, not just true for housing.

The HAFF should be radically expanded to be a $100 billion fund comprising such fund as a Submarine Future Fund (SFF) and a 2023 Olympics Future Fund (2032OFF). Strangely, housing is subject to this financial trickery, but other types of public spending is not. This suggest that the HAFF is designed to not spend money on public housing but look like a lot is being spent, hitting a political sweet spot.

What happens if the fund loses money?

It is unclear from the HAFF Bill what happens if the fund loses money. The Future Fund, for example, declined in value 1.4% in 2022 financial year. If the HAFF were to also see a decline in value, would this preclude any spending from the fund on actual new public housing?

This needs to be resolved.

After the 2008 financial crisis, the total value of Australian superannuation accounts fell around 20%, taking many years to recover. This is a risk that does not seem to be factored into the HAFF Bill. It is not clear why the Australian government needs to be exposed to financial market risk as a condition of investing in public housing programs.

Also, the economic cost in terms of managing this fund is quite high. The Future Fund currently pays 0.2% in overhead costs per year (about $500 million), so for the $10 billion HAFF that would be about $20 million per year in management costs alone.

Yes, the annual management cost of the Future Fund is the same size as the maximum amount available from the HAFF to spend on housing Australians.

Houses are assets too. Why not invest directly in building them?

Australian residential property is a high-return asset class popular with private investors, but very unpopular with governments. Public housing managers in each state own the equity of an enormous property portfolio worth billions, with values growing on average 7.8% per year, or a similar amount to the Future Fund's net returns.[1]

In the past five years the total value of Australia's dwellings increased from $6.78 trillion to $9.67 trillion. The average market value of each dwelling increase by 7.7% per year, exactly matching the Future Fund returns over the period.

So valuable are these capital gains on Australian housing that private investors are willing pay a price that makes them lose money each year in order to get future capital gains. This is the exact same investment situation as a public housing agency.

If investing in Australian housing is good enough for private investors, then it should be good enough for a government starting a housing fund.

How will fund returns be spent?

The HAFF Bill appears to contain little direction on how grants from the HAFF are to be spent.

What it does do limit the ability for Ministers to spend more than the $500 million dollar cap using the HAFF. It also incentivises Ministers to spend on housing programs when stock-market returns and HAFF returns are high, not when they are low. But ideal housing spending policy is probably the opposite, being counter-cyclical in nature to support housing construction when private markets are in a downturn.

Apart from the timing and amount of grants from the fund, the nature of the spending is important.

I argue that the most cost-effective way to spend money to get below-market rentals for residents is to build new public housing.[2] This is well known and was the finding of the 1989 National Housing Policy Review, the 1993 Industry Commission inquiry report into public housing.

Investing fund returns in rental subsidy schemes is not cost-efficient.

Ideally, the HAFF legislation would ensure money is predominantly spent on building and buying more public housing, rather than subsidising private rentals.

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[1] See for example Murray C, and P. Phibbs. 2023. *Reimagining the Economics of Public Housing at Waterloo.* OSF Preprints. February 27. doi:10.31219/osf.io/s5jc8

[2] See Murray, C. K. *Public housing is way cheaper than rental subsidies.* Fresh Economic Thinking. March 2022. https://fresheconomicthinking.substack.com/p/public-housing-is-way-cheaper-than