REVIEW OF THE NATIONAL HOUSING & HOMELESSNESS AGREEMENT

Submission from Master Builders Australia

March 2022

Executive Summary

Master Builders Australia welcomes the opportunity to provide a submission to the Productivity Commission's review of the National Housing & Homelessness Agreement (NHHA). Master Builders Australia is the nation's peak building and construction industry association which was federated on a national basis in 1890.

Latest figures indicate that Australia's construction industry is one of the largest sectors of the economy, directly accounting for 10.2 per cent of GDP and employing around 1.2 million people. Over many years, construction has consistently provided more full-time jobs and supported more small businesses than every other sector. Over the year to September 2021, work began on 228,000 new homes across the country - a volume of output large enough to house about 475,000 Australians.

Much of Australia's future housing stock will be built by Master Builders members over the years ahead. Previous decades have taught us how difficult it is for housing supply to fully keep up with demand. This imbalance is the main reason behind deteriorating housing affordability and poor outcomes related to housing provision generally. Looking ahead, we believe that future iterations of the NHHA should work to deliver better housing market outcomes by:

- Significantly reducing the cost of creating new homes
- Speeding up the delivery of new dwelling stock.

The issues contributing to high home building costs and lengthy construction times are complex. However, state, territory and local governments have considerable influence in areas like residential land supply, zoning decisions, the planning process and housing infrastructure costs. Demand substitution means that improvements in one section of the housing market will yield indirect benefits to most other parts of the market too.

- The next round of the NHHA should measure much more closely the performance of governments with respect to the components of the housing supply pipeline for which they have direct responsibility.

- Financial payments to the states and territories under the next NHHA should be conditional upon their achieving improvements to those elements of the housing supply pipeline under their control.
- Consideration should be given to the inclusion of local governments as parties to the next NHHA in order to incentivise improvements with respect to planning, development and building approvals as well as infrastructure contributions.

In addition to these suggested modifications, we also believe that the design of the next NHHA should try and facilitate several objectives.

- The scope and frequency of official data collection should be increased, particularly with respect to the residential land supply pipeline, zoning, approval times, developer contributions, homelessness and stock/flows relating to social and affordable housing.
- Converting data sources into a spatial housing settlement plan to provide a clearer picture of the shape of housing in Australia so as to determine where the need for government investment in housing is.
- Stamp duty surcharges on investment by non-residents in delivering new housing stock in Australia should be eliminated.
- Greater support should be given towards the development of Residential Real Estate Investment Trusts (REITs) in Australia so that more new housing supply can be unlocked.
- Obstacles to institutional investment in new housing (including by superannuation funds) should be identified and investigated with a view to being dismantled.
- States and territories should be encouraged to totally eliminate stamp duty on the building or purchase of a new home by first home buyers.
- The next NHHA should seek to deepen housing industry capacity in regional markets and address issues with the flow of housing credit in housing markets with lower turnover.

- The updated agreement should also explore whether incentives for improving the quality of relevant rental accommodation could be provided, including capital works which enhance a home’s energy efficiency and accessibility.

Master Builders Australia believes that the next National Housing & Homelessness Agreement has a huge role to play in improving housing supply and affordability outcomes and bettering the lives of all Australians in the years ahead.

Introduction

This submission relates to the Productivity Commission's review of the National Housing & Homelessness Agreement (NHHA) which we understand is due for completion by the end of June 2022.

The National Housing & Homelessness Agreement (NHHA) commenced on 1st July 2018 and is scheduled to run for a 5-year term which will expire at the end of June 2023. It is an agreement between the Australian government and the eight state and territory governments and relates to the provision of housing and homelessness services. NHHA is one of a set of national agreements which were established in the wake of the 2008 *Intergovernmental Agreement on Federal Financial Relations*.

At present, the Australian government provides about $1.6 billion per year to the states and territories with the aim of improving Australians' ability to access affordable, safe and sustainable housing. Of this, $129 million is dedicated to homelessness services an amount which the states and territories must match in full.

In return for receiving these funds from federal government, the state and territory governments are required to have publicly-available housing and homelessness strategies. The Agreement also binds the states and territories to delivering improvements with respect to data collection and reporting.

Background to Master Builders Australia and our industry

About Master Builders Australia

Master Builders Australia (Master Builders) is the nation's peak building and construction industry association which was federated on a national basis in 1890. Master Builders' members are the Master Builder State and Territory Associations.

Over 130 years, the movement has grown to over 32,000 businesses nationwide, including the top 100 construction companies. Master Builders is the only industry association that represents all three sectors, namely residential, commercial and engineering/civil construction.

Australia's building and construction industry

Building and construction is one of the largest sectors of the Australian economy. Latest ABS figures indicate that the total value of building and construction work done during 2021 totalled $221.6 billion in value, an amount directly equivalent to 10.2 per cent of total GDP.

Our industry packs its biggest punch when it comes to the provision of full-time employment and support for small business. During November 2021, there were 1.15 million people employed in the building and construction industry. About 85 per cent of these jobs were full-time in nature, a far higher proportion than in the rest of the economy. This means that construction has consistently been the economy's largest provider of full-time jobs over many decades. During November 2021, there were 967,000 full-time jobs in the construction industry – more than every sector of the economy outside of health.

The most up-to-date ABS data indicates that as at 30 June 2021, there were a total of 410,763 construction businesses in operation across Australia. This is more than every other sector of the economy. The most striking feature of our industry's construction businesses is their size: of the total, the overwhelming majority (98.6 per cent) are small in size with less than 20 employees. More than half of our construction businesses (56.5 per cent) have no employees at all, typically operating as sole traders or partnerships.

The small size of construction businesses is reflected in their pattern of turnover. The majority (58.5 per cent) turn over less than $200,000 per year with about 1 in 5 (20.9 per cent) earning less than $50,000 annually. Just 1.4 per cent of building and construction businesses have annual revenues in excess of $10 million.

The structure of construction activity means that the support offered by it to other parts of the economy is strong. This is because there is a high domestic content to our industry's inputs including building materials, labour and professional services. As a result, it is estimated that for every $1 million worth of residential building activity the entire economy is better of to the tune of $3 million. Similar, $1 million worth of building and construction activity is estimated to support a total of 9 full-time jobs across Australia's economy – including 3 jobs in other sectors outside of building and construction.

In terms of our industry's outputs, about $94.0 billion worth of civil and engineering construction was carried out during 2021. In addition to this, residential building work totalled $78.7 billion during the year with $48.9 billion worth of non-residential building work done during 2021.

Latest figures show that work started on about 228,000 new homes over the year to September 2021, of which 149,300 were detached houses. Over the same period, almost 183,000 new homes were completed and became available to live in for the first time – meaning that a roof was put over the heads of about 475,000 Australians.

Over this 12-month period, building work began on 3,762 new units of public housing – an increase of +37.2 per cent on one year earlier. However, the share of new home building accounted for by the public sector is quite low by historic standards and this represents a key challenge.

The building and construction industry is at the fulcrum of mentoring our nation's next generation of trades workers. During 2020-21, a total of 17,650 new apprenticeships were completed with a further 50,760 new construction apprentices and trainees beginning their journey. As at 30 June 2021, a total of 111,465 construction industry apprentices were in training. Encouraging, apprentice involvement in the industry has grown strongly over the last couple of years thanks to enhanced government support programs as well as favourable business conditions in the industry.

Outlook for residential building to 2025-26

2020-21 has just gone down as the strongest year on record for new detached house starts. Over the year to June 2021, work began on a total of 138,480 new houses across Australia. This was 35.6 per cent higher than the previous financial year and shatters the record previously held by 1988-89 are being the busiest ever for new detached house building.

The HomeBuilder scheme has been the main catalyst for the surge in house building. The scheme was unveiled in June 2020 and remained open until the end of March 2021, with qualifying work permitted to commence up to 18 months after the contract date. This means that HomeBuilder-supported work will continue to kick off until late September 2022 with the last of these jobs likely to reach completion in early 2023. In total about 113,000 HomeBuilder applications have been made in relation to new builds, of which over 64,000 have been granted to date.

HomeBuilder’s effectiveness in spurring new home building has been bolstered by a number of other favourable factors. For example, mortgage interest rates are at very low levels by historic standards, a situation which has helped demand. Low interest rates have also reduced financing costs for builders and developers and helped support the supply of new homes.

The shift in consumer preferences towards larger homes has also contributed to record levels of new detached house building. The pandemic has forced people to spend significantly more time at home and this has induced what may prove to be a permanently increased appetite amongst homeowners for more floor space. Also, people’s home location is not as tightly linked to their place of work as before and this has allowed some professions to base themselves in regional areas and still work for CBD-located businesses. With detached houses generally accounting for a much greater share of regional dwelling stock compared with large cities, this change has also been of benefit to detached house building.

The high-water mark reached by detached house building during 2020-21 inevitably means that activity is currently retreating. Latest building approvals show that the number of approvals for new detached houses dropped by 18.3 per cent during the

September 2021 quarter, although the pipeline is still well higher than a year earlier. We project that detached house building starts will drop by 18.0 per cent during 2021-22 overall. However, the volume of new detached housing output will remain quite elevated by comparison with historic norms. By the end of our forecast horizon in 2025-26, we anticipate that 117,500 new detached houses will be started.

The return of investor confidence as well as more normal levels of internal migration to Australia is good news for higher density home building. This side of the market had been on the slide well before the pandemic. Unsurprisingly, the pandemic caused the medium and high-density home building slump to deepen amidst negligible inward migration to Australia and much greater reluctance amongst developers to take on the risk burden associated with larger projects. However, there was a modest (+3.0 per cent) increase in medium and high-density dwelling starts during 2020-21 with the year’s total reaching 72,100.

During the September 2021 quarter, the number of new medium-high density building approvals was 34.3 per cent up on the same period a year earlier. Growth was slightly stronger amongst high density approvals (+36.7 per cent) compared with those in the medium-density category (+29.2 per cent). Our expectation is that growth will continue with medium-high density dwelling commencements set to expand by another 6.8 per cent during 2021-22 and top 87,700 by the end of our forecast horizon in 2025-26 – some 21.7 per cent higher than in 2020-21.

Over the year to September 2021, the average new home building approved was $338,470. Interestingly, new high-density homes had the largest approval value ($389,500) over this period followed by new detached houses ($331,150). On average, new medium-density homes averaged $307,840 over the year to September 2021.

Home renovations activity is also set to perform quite strongly over the next few years. Thanks to the combination of HomeBuilder support and a host of favourable macroeconomic factors including low interest rates and very strong house price gains, the volume of home renovations activity rose by 13.8 per cent during 2020-21. Activity is likely to retreat marginally (-0.3 per cent) in 2021-22 but further expansions are then anticipated to take hold over the following three years. This will be helped by the age profile of the housing stock with large numbers of detached houses entering the prime renovations age bracket over the next couple of years. By 2025-26, the volume of home renovations work done is predicted to be 5 per cent higher than the record high achieved during 2020-21.

Taking the three strands of residential building together, the outlook for the next five years is quite favourable. The switch away from detached houses and towards higher-density home building combined with the sustained success of home renovations activity means that the volume of residential building activity is likely to expand by a further 10.8 by 2025-26 – on top of 2020-21's already impressive level of activity.

While this represents our best forecast of what might eventuate, it is important to be conscious of some of the risks faced by residential building over the next few years. The continuation of strong home price growth brings with it the possibility that prices could decelerate in a rapid and disruptive manner. There is also scope for intervention by financial regulators aimed at soothing home price pressures. Any such measures could include limits on certain types of mortgage lending deemed to be higher risk. These restrictions could be targeted at loans with higher Loan-Valuation Ratios or those involving Loan-to-Income multiples above certain thresholds. Interest-only mortgages or those to investors could also be the targets of any restrictions.

Within the macroeconomic sphere, there is also the risk that it could take a long time for inward migration to revert to the kinds of volumes typical of the pre-pandemic era (200,000 to 250,000 per year). Whether this happens partly depends on how well Australia's labour market bounces back from the damage inflicted during the lockdowns of 2021.

Master Builders response to issues

In line with the structure of the Productivity Commission's Issues Paper, the substance of our submission is divided into three major components which look at:

- Assessing the performance and suitability of the Agreement;
- Issues across the housing spectrum; and
- The supply side of the housing market.

Our inputs to this submission focus on the aspects of the review where we can best make a meaningful contribution. This includes issues like housing affordability, the process of creating new dwelling stock, taxation, incentives, land supply, zoning and regulation amongst others.

Assessing the performance and suitability of the Agreement

The roles and responsibilities of governments under the Agreement

As outlined in the Productivity Commission's issues paper, local governments have an influence over important aspects of the process of creating new homes including local planning, infrastructure provision and developer contributions. These issues have a major impact on the timing and costs of new housing stock and performance improvements in these areas would yield significant benefits in the areas of housing affordability and provision. Accordingly, we believe that consideration should be given to including local governments in the next iteration of the NHHA so that improvements in their processes can be delivered through the use of financial incentives from federal government.

Performance monitoring and reporting

In Australia, much of the official data on building activity is of a high standard. For example, figures on building approvals are produced monthly and offer a high degree of geographic disaggregation. There is also a comprehensive breakdown available of the types of new dwellings being approved as well as information on major home renovations. On the non-residential building side, figures are published for no less than 15 subcategories. This is a very valuable resource which is worthy of acknowledgement.

There remain some very substantial gaps in the availability of data with respect to important components of the development pipeline for new housing, including those in the social and affordable category. In short:

- There is a lack of nationally-consistent data on the volumes of residential land being navigated through the development pipeline;
- Data on the stocks and flows of social, community, affordable and public housing is insufficient.

Working to eliminate these data gaps is important because it would allow us to gain a much better understanding of the land development process and help pinpoint where bottlenecks and other unnecessary delays exist. In terms of the specific mandate of the NHHA, a wider set of data and complementary production of a national housing settlement spatial plan would allow the federal government to specify more precise performance goals to the states, territories and local governments that sign up as counterparties to any future agreement(s).

Significant data gaps exist with respect to the residential building pipeline. These gaps prevent us from pinpointing the more urgent areas for action. They also make it much more difficult to know whether or not progress is being made over time. Improvements here would illuminate our understanding of the affordability problem and improve the likelihood of delivering solutions. We currently lack adequate data on:

- The volume and price of land at all stages in the residential pipeline in all eight jurisdictions.
- The time taken for land and new home building projects to navigate important processes like zoning, planning milestones, development approval and building approval.
- The numbers of new homes being built annually in the social, community and affordable housing spheres.
- NHFIC found that 'there is no publicly available aggregated data on developer contributions across most states and territories.' Accordingly, a centralised, harmonised and comparable national database of each local government area's developer contribution receipts and pricing behaviour would allow for

performance to be gauged and the models of best practice to be identified and learned from.

Financial and governance arrangements

Federal government needs to tie financial payments to improving the performance of lower tiers of government in areas affecting the cost and timing of new home building. It would be a good step if the future design of the NHHA linked payments to the states/territories to the effectiveness of their performance when it comes to zoning and planning. As outlined above, local governments hold some very important reins when it comes to the delivery of new housing supply and we believe that consideration should be given to the use of incentive payments in order to lift their performance in these areas.

Data provision related to social housing stock

The usage of the terms social housing, public housing and affordable housing can be conflated and confusing, so at the outset it is important to be specific about their precise meanings as used in our analysis.

Social housing is an umbrella term for three mutually exclusive categories of housing. These are:

1. Public housing which is directly owned and managed by the state and territory governments

2. Community housing which is managed by not-for-profit Community Housing Organisations (CHOs)

3. Indigenous housing.

In general, all three types of housing are allocated to tenants on the basis of tenant need with the rental charge typically set below market rates in a manner designed to be affordable to the tenant. For example, the rent charged by the provider will take into account the tenants' income and other characteristics so as to ensure that the rent is manageable from the perspective of tenants. These means that tenants with lower incomes will usually pay smaller rents.

A simple categorisation of Australia's housing stock is set out in the diagram below.

<table>
<tr><th colspan="5">Simplified categorisation of Australia's social and private sector housing stock, March 2022</th></tr>
<tr><td rowspan="6">Total stock of housing</td><td rowspan="3">Social housing</td><td colspan="2">Public housing</td></tr>
<tr><td colspan="2">Community housing</td></tr>
<tr><td colspan="2">Indigenous housing</td></tr>
<tr><td rowspan="3">Private sector housing</td><td colspan="2">Owner occupied</td></tr>
<tr><td rowspan="2">Rented by private landlord</td><td>Rent set at discount to market rate ('affordable')</td></tr>
<tr><td>Rent set at full market rate</td></tr>
<tr><td colspan="5">Source: Master Builders Australia analysis</td></tr>
</table>

The table above lists most of the potential means by which the stock of social housing can increase or decrease. Collecting as much data about each of the categories in the table as possible would allow for the stock of social housing to be monitored as effectively as possible.

In addition to data collection, mapping housing settlement outcomes in a national housing settlement spatial plan would provide a much clearer picture of the shape of housing in Australia to determine where the need for government investment in housing is.

Summary of potential inflows and outflows to/from Australia's stock of social housing	
Inflows (+)	**Outflows (-)**
New homes built for use as Social Housing	Demolition of Social Housing stock
Private sector homes purchased for use as Social Housing	Social Housing stock sold to private ownership
Non-residential buildings converted for use as Social Housing stock	Social housing stock converted to non-residential use
Private short-term accommodation stock acquired for use as social housing	Social Housing stock converted short-term accommodation usage
Social Housing stock rented from private sector market	Social Housing stock placed on private rental market
Existing Social Housing stock subdivided into more units	Existing Social Housing stock combined into fewer units
Source: Master Builders Australia analysis	

For example, no state or territory government routinely publishes statistics on the construction of new social and affordable housing, nor on public housing sales or demolitions. Similarly, there is no national statistical information on community housing construction.

Issues across the housing spectrum

This part of our submission explores several topics. These include:

- Homelessness
- The private rental market
- Home ownership
- Housing outcomes for Aboriginal and Torres Strait Islander people

These are detailed in turn over the sections which follow.

Homelessness

As set out in the Issues Paper, about 1 in 200 Australians were defined as homeless in 2016, the latest date for which a reliable estimate is available. Ominously, there was a significant jump in the number of homeless Australians between the Censuses of 2011 and 2016.

Master Builders Australia regards every case of homelessness as one case too many. Homelessness is the most extreme manifestation of housing policy failures and making significant inroads into eliminating the issue is something that is a huge matter of urgency.

We acknowledge that the tragedy of homelessness is a very complex one and that the pathways to eventual homelessness for individuals and their families can be very diverse. Master Builders builder members have a vital role to play in delivering the additional dwelling stock required to put a roof over the heads of those currently lacking shelter. As alluded to elsewhere in this report, we believe that speeding up the pace of creating new homes through eliminating regulatory and bureaucratic obstacles is one way to achieve this.

It is also our view that the funds of the governments and other organisations who directly provide shelter to those who are homeless could go much further if some of our proposals on reducing the costs of creating new homes were taken up. Doing so would allow for more people to be taken off the homeless list each and every month.

As with other areas of our submission, we are also supportive of measures to expand the range and timeliness of data collection when it comes to those affected by homelessness. We note that Census 2016 serves are the most recent gauge of some aspects of our homelessness issue. Better data would aid our understanding of the specifics of the problem and allow for our responses to be fine-tuned much more effectively.

The private rental market

As noted in the issues paper, the private rental market is a source of housing for about 2.5 million Australians. The private rental market is often the first step for those departing from reliance on social housing. For some, accessing housing needs through the private rental market is a temporary step along the road to eventual home ownership. Others will be permanently housed by the private rental market as a matter of preference or because they are unlikely to ever be in a position to purchase a home of their own.

In terms of achieving favourable outcomes in the rental market, we believe that the current arrangements around negative gearing and capital gains tax allow rental accommodation to be provided to tenants at much lower cost than would be the case in their absence. We believe that their permanent retention.

Leveraging different classes of investor funding in order to expand the supply of accommodation to the rental market would help improve housing affordability and lead to better outcomes in the housing market. There are currently barriers to this which could be removed. For example, almost every state and territory government has imposed enormous stamp duty surcharges on purchases of residential property by foreign investors. Consideration should be given to removing these for newly-built homes so that foreign investor capital could be successfully used to support the creation of new homes for people to rent.

There are other potential mechanisms for expanding the supply of housing on the rental market. Residential Real Estate Investment Trusts (REITs) have a very limited footprint in Australia at present. REITs would allow for ordinary investors to hold a slice of Australia's housing market in a low-cost manner and without having to take on any borrowings at all. The residential REIT in which they hold shares would own and rent out accommodation on the rental market, a portion of which would be paid out to investors as a dividend once costs are deducted. Promoting the development of residential REITs in Australia should be examined in detail by government, particularly when it comes to the scope for residential REITs to support the building of new housing stock.

In addition to residential REITs, there are also opportunities for large-scale institutional funding to deliver additional housing in the private rental market. In particular, the scope for superannuation funds to operate here is enormous. Serious consideration needs to be given to fully investigating why institutional involvement here is currently so limited and what changes can be made in order to expand this potential source of new housing stock across Australia.

The quality of the current rental housing stock has an important impact on the well-being of those who live in it. The current design of the taxation system means that the financial incentives for making improvements to rental accommodation are very small, with capital works only deductible over a 40-year horizon. One way is which this could be remedied is by providing more favourable tax treatment to capital spending targeted at improving the quality and performance of rental stock. This might include capital works which enhance the energy efficiency and accessibility of homes on the rental market.

Home ownership

Playing our part in helping people to own their own home for the first time is one of the most rewarding elements of the building industry's work. Permanently owning one's home provides a great deal of emotional satisfaction and security. It also allows for the roots of communities to be deepened and for neighbourhoods to flourish. In terms of individual well-being, housing costs plummet later in life once the mortgage has been fully repaid. In contrast, those who rent permanently will be faced with regular expenses related to housing in perpetuity. This was corroborated by the Grattan Institute in 2018, which found that "senior Australians who rent in the private market are more likely to suffer financial stress than homeowners, or renters in public housing."[1]

Sadly, the dream of home ownership gets further and further away for successive generations of Australians. Earlier, we discussed how the inability of housing supply to

[1] Grattan Institute (2018) "Money in retirement – more than enough" (John Daley and Brendan Coates)

keep up with demand results in the price of homes consistently outgrowing wages and earnings across the economy.

It is outlined earlier in our submission how the cost of producing new homes can be reduced and why we need to strive to deliver our new dwelling stock much more quickly. Progress on both these fronts would help bring home ownership within reach for many more Australians.

We acknowledge the work over recent years by the federal government and by NHFIC in assisting first home buyers through such schemes as the First Home Loan Deposit Scheme as well as HomeBuilder.

Going forward, we believe that both federal and state/territory government interventions to support first home buyers should be designed in a way that addresses the root problem, namely that housing supply needs to keep up more closely with demand. Accordingly, more attractive incentives should be offered to those first home buyers wishing to build or buy a new home. As well as benefitting the individual first home buyers' affordability situation, designing incentives in this way will result in more new homes getting built sooner.

For the same reason, consideration should be given by all eight state and territory governments to permanently eliminating stamp duty on the construction or purchase of newly-built homes by first home buyers by the end of the next NHHA term. In all cases, we believe that the best progress in addressing the problem lies in focusing first home buyer schemes on those building or purchasing new homes.

In terms of the impact of Covid-19 on housing demand, there has been an increased demand for more spacious types of housing including detached houses. The feasibility of living in regional parts of Australia has been enhanced by much greater scope for working from home and remote working arrangements. As a result, we have seen a remarkable situation whereby home prices in regional markets have outgrown those in the capital cities for much of the past two years.

Housing outcomes for Aboriginal and Torres Strait Islander people

The big switch from living in the major cities in favour of regional areas has brought into sharper focus some of the difficulties faced by those seeking appropriate housing in regional markets for many years.

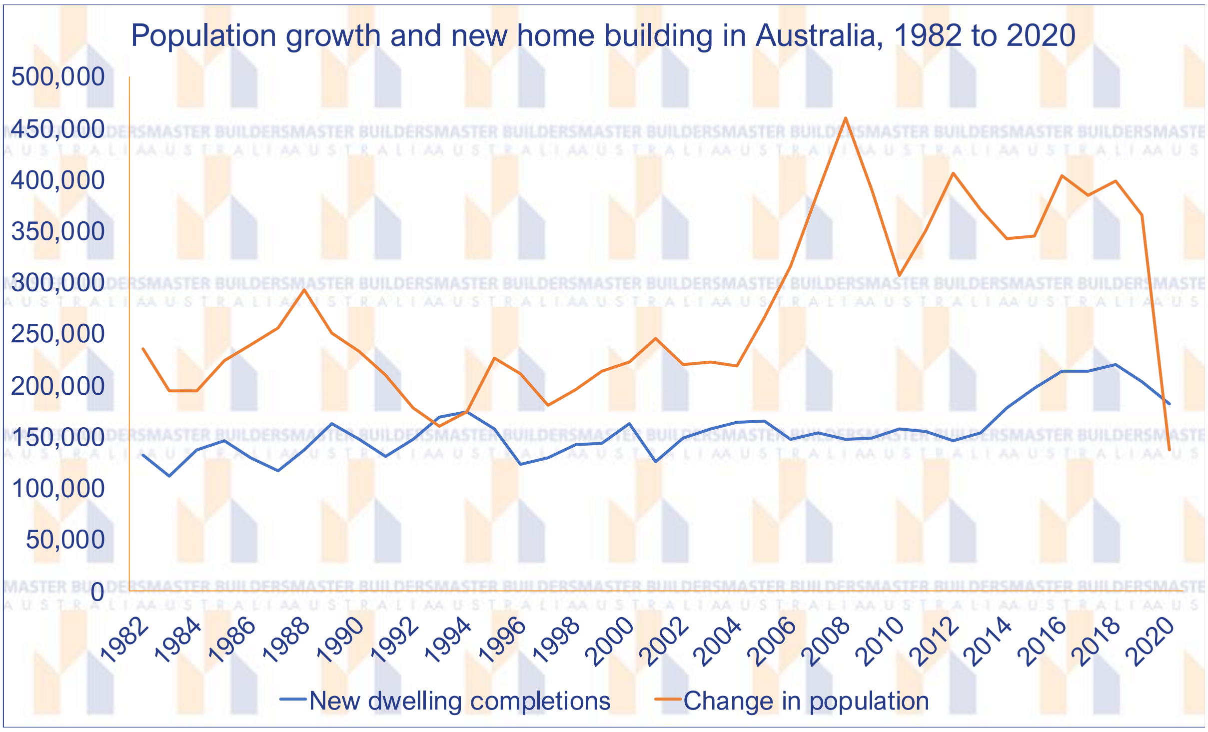
Industry capacity is the first obstacle to ensuring that enough of the right types of housing gets built in smaller regional markers. The skilled workforce capacity is the most important resource available to the home building industry in regional markets. The pool of available workers is typically small, and geographic isolation means that the scope for bringing workers in from other regions can be limited and economically unfeasible. Because wage rates are usually higher in capital cities than in regional areas, there is a constant risk of trade workers in regional areas departing to larger cities in order to boost their earnings. The struggle to maintain a large enough workforce in regional markets makes it much more difficult to deliver the housing needs of all those who live there.

A second issue affecting home building activity in regional markets relates to financing. In capital cities, turnover in the housing market is high. As a result, the volume of up-to-date data on prices in the local market is substantial and valuations can be performed with a fairly high degree of accuracy.

In contrast, regional markets see much fewer housing transactions and this makes it much more difficult for valuers and financiers to pinpoint the likely market value of residential land and homes. This sometimes leads lenders to take a more cautious approach when providing debt finance for the construction or renovation of homes in regional markets. This can prevent new home building projects from proceeding at all, or result in projects being completed on a smaller scale than desired. Either way, the housing needs of those living in regional Australia end up being underserved.

The supply side of the housing market

Over recent decades, the supply of new homes has consistently fallen short of the needs of a growing population (see chart below). The is the main reason why dwelling prices have outgrown both incomes and prices across the economy for a very long time.



The past decade has starkly illustrated how difficult it is for the supply of new homes to meet the strong demand for them. For the first time since modern records began, new home building starts exceeded 200,000 per year over the five-year period between 2014 and 2018, with a record volume of new homes being made available to the market over this period. On top of this, the announcement of the HomeBuilder scheme in June 2020 resulted in new detached house building starts stretching to their highest level on record with 150,000 new starts over the year to September 2021.

Despite this unprecedented level of new housing output, dwelling price growth has still been rapid. At its peak during 2021, the pace of house price growth nationally reached its fastest rate since 1988. Latest data from CoreLogic indicates that house prices rose by 24.9 per cent across Australia’s eight capital cities over the year to February 2022, with prices in regional Australia growing even more quickly (+30.7 per cent) over the same 12-month period. These huge price gains occurred even though Australia was experiencing its first population fall in over a century at the same time.

With inward migration to Australia set to recover to normal levels over the near term, there is a real risk that housing affordability could worsen even further. We do not believe that the solution lies in restricting inward migration to Australia given the increasingly vital role played by migrant labour in driving growth in living standards over the long term.

Rather, we believe that preventing further deteriorations in housing affordability will require extraordinary efforts on the supply side of the equation. Any supply side interventions in the market should be geared towards two overarching objectives:

1. Reducing the cost of creating new homes
2. Shortening the amount of time it takes to deliver new units of housing supply.

In the absence of improvements here, it is likely that housing supply will fail to fully keep up with demand over the years and decades ahead with the result that housing affordability deteriorates even further.

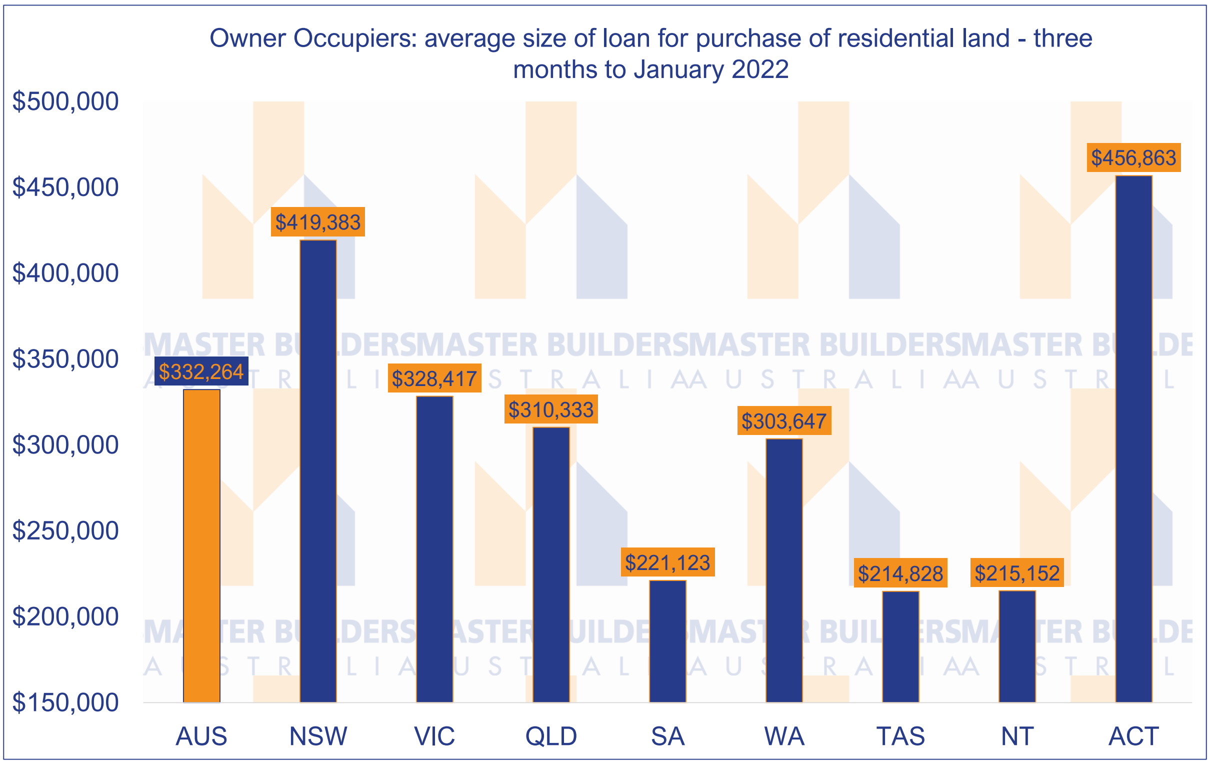
A range of things go into creating newly built homes: land, government resources, materials, labour, professional services, risk, entrepreneurship and the need for a reasonable rate of financial return.

Market failures exist in some areas of the housing market, including social/affordable housing and some regional markets where capacity is thin.

Planning and land use regulation

In the vast majority of cases, residential land is the single biggest ingredient of every new home. No other input to the new housing production equation has such a massive effect on both the price and the eventual volume of new home supply. There is a lack of completeness and comparability when it comes to residential land data in each of the jurisdictions. Some degree of comparison can be gained by comparing the average loan size for residential land purchase. As the chart below illustrates, the average loan came to over $332,000 nationally over the three months to January 2022. Based on this metric, the most expensive land lots are in the ACT ($456,900), New South Wales

($419,400) and Victoria ($328,400) with the lowest land costs in Tasmania ($214,800) and the Northern Territory ($215,150).



In terms of the effect of the residential land market on housing affordability, there are a number of major issues:

- Governments and public entities often have dominance of the supply for greenfield (i.e. undeveloped) land. Like all monopolistic market structures, there is a natural tendency towards outcomes involving excessive greenfield land costs, and supply ending up being insufficient relative to demand in the market.
- A conflict of interest is also at play with respect to governments and their role as suppliers of land. If governments were to release more of their land holdings to the market, it is likely that land price growth would decelerate. This would have the effect of slowing down the pace of increase in council rates and land taxes (which are calculated based on land prices) and hurt state/local government revenue streams. Thus, measures which advance housing affordability could prove costly for a government's own financial situation.
- As with other areas of the new housing production line, there are serious issues with the collection and publication of data relating to the residential land market.

> While adequate figures are available for some jurisdictions, the lack of a nationally consistent set of figures relating to the volume of land at different stages of the pipeline and information relating to transaction volumes and sales price in the market means that any future improvement (or deterioration) will be difficult to detect.

Before any work can begin on developing land, it must first receive the necessary zoning from the relevant authority. From the developer's point of view, this can be a time consuming and financially expensive process. Like land supply, the calculus of zoning decisions made by governments can be clouded by the fact that its own revenue streams benefit from higher residential land prices.

The relevant zoning authority is also encumbered with monopoly power in the market it oversees. This protected situation means that there is a much greater likelihood of poor outcomes concerning delays, inefficiencies, costs and service. All of these outcomes hamper the supply of new housing and contribute to substantially higher zoned land prices.

Like the zoning process, the procedure for receiving development or building approval can be fraught with hurdles and delays. Local government planning departments are also susceptible to the difficulties that can result from organisations operating in a monopolistic fashion, as outlined above.

Changes need to be made in order to reduce the cost of creating the new homes which we need.

Federal governments need to tie financial payments to improving the performance of lower tiers of government in areas affecting the cost and timing of new home building. It would be a good step if the future design of the NHHA linked payments to the states/territories to the effectiveness of their performance when it comes to zoning and planning.

Doing this properly will require an expansion in the collection of consistent data, an issues discussed in more detail above.

Inclusionary zoning requirements

As alluded to earlier in our submission, the absence of comprehensive data on the stocks and flows of social, affordable and community housing make it difficult to provide a definitive answer to the question.

Our view is that housing affordability can be improved in almost all price points of the market by reducing the cost of creating new homes and through delivering new housing stock more quickly. The degree of interlinkage between the different tiers of the housing market means that improvements in affordability in one part of the market are likely to produce better affordability outcomes in other parts of the market over time. This is because the demand for housing will swing towards the section of the market where affordability has improved, resulting in less demand for other parts of the market. This effect will tend to depress rents and prices in the parts of the market experiencing an exodus of demand. In this way, affordability improvements which are initially narrow will tend to spread out to wider parts of the market. Accordingly, it is our view that rents and supply in the affordability and social area of the housing market will occur whenever housing supply is increased across the board due to the effect on prices of displaced demand.

When it comes to the economics of creating new homes, the risk-reward calculus of developers and builders is central to determining how expensive the final housing product will be. In general, restrictions and stipulations like Inclusionary Zoning Requirement (IZRs) are unwelcome from the point of view of builders and developers because they potentially restrict the way new housing developments proceed. This increases the likelihood that the project may not proceed at all or on a smaller scale than previously envisaged.

NHHA performance indicators

Monitoring the process of zoning and planning is vital for identifying best practice and whether performance is getting better or worse over time. Accordingly, we welcome the use of the performance indicators set out in the Issues Paper, namely:

- Number of dwellings permitted by zoning; and
- Time taken to decide development applications.

As we set out earlier in our submission, we believe that gathering as much data as possible relating to the volumes of land/housing traversing milestones in the planning process as well as the time taken for this to occur would be hugely beneficial. We are also of the view that publishing this data on a detailed and nationally-consistent geographic basis (by state/territory and local government area as appropriate) and producing a geospatial national housing settlement plan, would serve an extremely useful purpose. The 'top' performers could be readily identified and learned from. Similarly, those governments delivering a subpar performance could be resourced and assisted with a view to making improvements.

There are numerous ways of measuring the degree to which housing need is being met in a particular geographic market. Monitoring the ratio of dwelling stock to population is generally an effective way of doing this. However, it is not a perfect measure as it does not take account of variations in the structure of the population which have important implications for housing demand. Different sections of the population vary in terms of how intensively they use housing.

For example, the housing needs of two different markets with exactly the same number of people but with different age structures would not be the same. This is because older populations use the housing stock more intensively than younger age cohorts due to the fact that average household sizes are smaller amongst older members of the population. In other words, it is possible that two different places which return the same 'score' on their dwelling stock/population ratio could have quite contrasting experiences in terms of the abundance of housing supply - depending on the age structure of their population. Such an issue could be remedied by using a so-called 'age standardised' ratio which would take account of differences in the structure of the population.

Suitable performance indicators should encourage effective actions from those being monitored. According, consideration should be given to measuring the relationship between new additions to the housing stock (say over the past five years) and the change in population (possibly in an age-standardised form) over the same period. This would encourage policy makers to target new home building output to fully match the needs of a changing population more closely.

Planning and land use policy constraints

We have detailed above some of the ways in which planning and land use policies by lower tiers of government cause unnecessary delays to the creation of new homes and how the homes which do get built are more expensive than would be the case under a more effective regulatory environment related to land use and planning.

The current regulatory environment generally constrains the development of all types of new housing across the spectrum, including those which are diverse and low-cost in nature.

The building and construction industry

Industry regulation

While some degree of regulation is necessary and welcome when it comes to residential building activity and its final outputs, the imposition of rules and restrictions has inevitable consequences for the cost of producing new homes.

For those in the residential building industry, some mandatory regulations have proven to restrict the way in which work can be performed. This means that more efficient and more cost-effective ways of completing projects may have to be dropped in favour of significantly more expensive techniques. The regulatory framework may also have the effect of preventing the delivery of some projects for which there is a willing market, and which would add to the supply of new homes. In short, regulation can sometimes get in the way of more affordable housing.

The overwhelming majority of building and construction businesses are small when it comes to turnover and the employee headcount: well over one half of businesses in our industry either do not have any employees at all or else turn over less than $200,000 per year (or both). This means that most building and construction firms do not have resources in the form of regulatory staff or departments. As a result, they struggle to cope with the existing body of regulations.

This problem is compounded by the fact that regulations are frequently changing with each change sparking off yet another round of costly and productivity-sapping modifications to the business models underpinning their operating a. There is a perception amongst industry participants that the net effect of regulatory change over time is resulting in a heavier rather than lighter regulatory burden.

For example, an updated National Construction Code (NCC) was released in 2019. The 2019 NCC consists of three volumes which in aggregate run to over 1,600 pages, providing detailed guidelines on the carrying out of building and construction work. An updated NCC will be released in 2022 and is expected to be of a similar calibre.

Currently there are significant changes proposed in regulations that respond to policy discord on climate change and the needs of people with mobility impairments that substantially alter construction methods for home building. These include:

- New energy efficiency requirements in construction of the home regarding thermal building fabric (glazing and insulation), space heating, cooling and ventilation, preparedness for renewable energy power supply and energy assessment of building work;
- Accessible housing design requirements for the entrance and ground floor amenities of a home that require more space when governments keep reducing the size of blocks for housing; and
- Development and updating standards for building homes in disaster prone areas.

While these changes are well intentioned, they are not given appropriate time to be developed and implemented effectively; or are not sequenced in a manner for industry to effectively absorb change. The benefits for the broader community in these reforms are lost because rushed and therefore poor regulation is not effectively implemented and enforced because of its complexity.

A further failing in the development of these regulations is disregard for the regulation impact assessment (RIA) processes. The federation of Building Ministers for example recently decided to procced with introducing new mandatory accessible housing design requirements for all new homes, despite the RIA identifying the cost-benefit did not stack-up.

The capacity of the construction industry to deliver homes in a cost-effective way is exacerbated in exceptional circumstances by regulated settings for fixed price housing contracts. In a normal market, this a not a problem. It becomes a problem in a market when costs arising from delays to the project, are from uncontrollable factors such as the issuance of public health orders, workforce and product shortages and supply chain disruption.

More flexible provisions where states regulate fixed price housing contracts are needed to enable the burden of unforeseen costs to be shared more equitably in exceptional circumstances. To mitigate the risk of workforce and product shortages, a more concerted effort by government is needed to develop more sovereign capability, target key import markets and support industry innovation in the construction sector.

For the hundreds of thousands of small construction businesses, the existing set of regulations and the stream of changes to them place represent a very major cost. This cost is not just paid in financial terms; getting to grips with regulations also exacts a substantial toll on the time, energy, well-being, mental health and relationships of the people and families who run Australia’s building and construction businesses.

In addition to the process of actually implementing regulations, the financial cost of acquiring the publications and manuals in which regulations are detailed can also be very substantial. For example, access to a set of 96 standards relating to the use of timber in buildings is currently being sold by Standards Australia at a cost of $507.59 for a 12-month subscription.

Far too often, new regulations are added based on their expected net marginal benefit. That is, proposed regulations are only evaluated based on the extra costs they are likely to impose, with the existing collection of regulation not being looked at. For those in business, this means that another unwelcome layer of regulation gets added to the already enormous mountain.

This problem is further exacerbated by the fact that new regulations can come from any one of a huge range of sources, including governments and regulatory bodies. There is often a failure by them to act in tandem, with the result that the interaction between different regulations deriving from separate authorities is often a further source of frustration and inefficiency.

To address productivity and subsequent cost impacts from regulation, Master Builders recommends the following:

- Future regulatory changes which affect building and construction activity be evaluated with respect to the aggregate cost of all existing regulations rather than just the marginal cost, however small, of proposed new regulations.
- Governments allow for more flexible provisions where states regulate fixed price housing contracts to enable the burden of unforeseen costs to be shared more equitably in exceptional circumstances.
- Introduce an effective whole of government process for taking a more holistic approach to boosting local capability in the construction supply chain to respond to government crisis and reform efforts. This relates to workforce, materials and infrastructure supply, skills and industry innovation.
- As in other areas, federal government funding between tiers of government and regulatory bodies should be linked to how those entities perform with respect to regulatory improvements. For example, the effectiveness with which regulators co-ordinate and share data with each other could be used to determine future funding allocations.