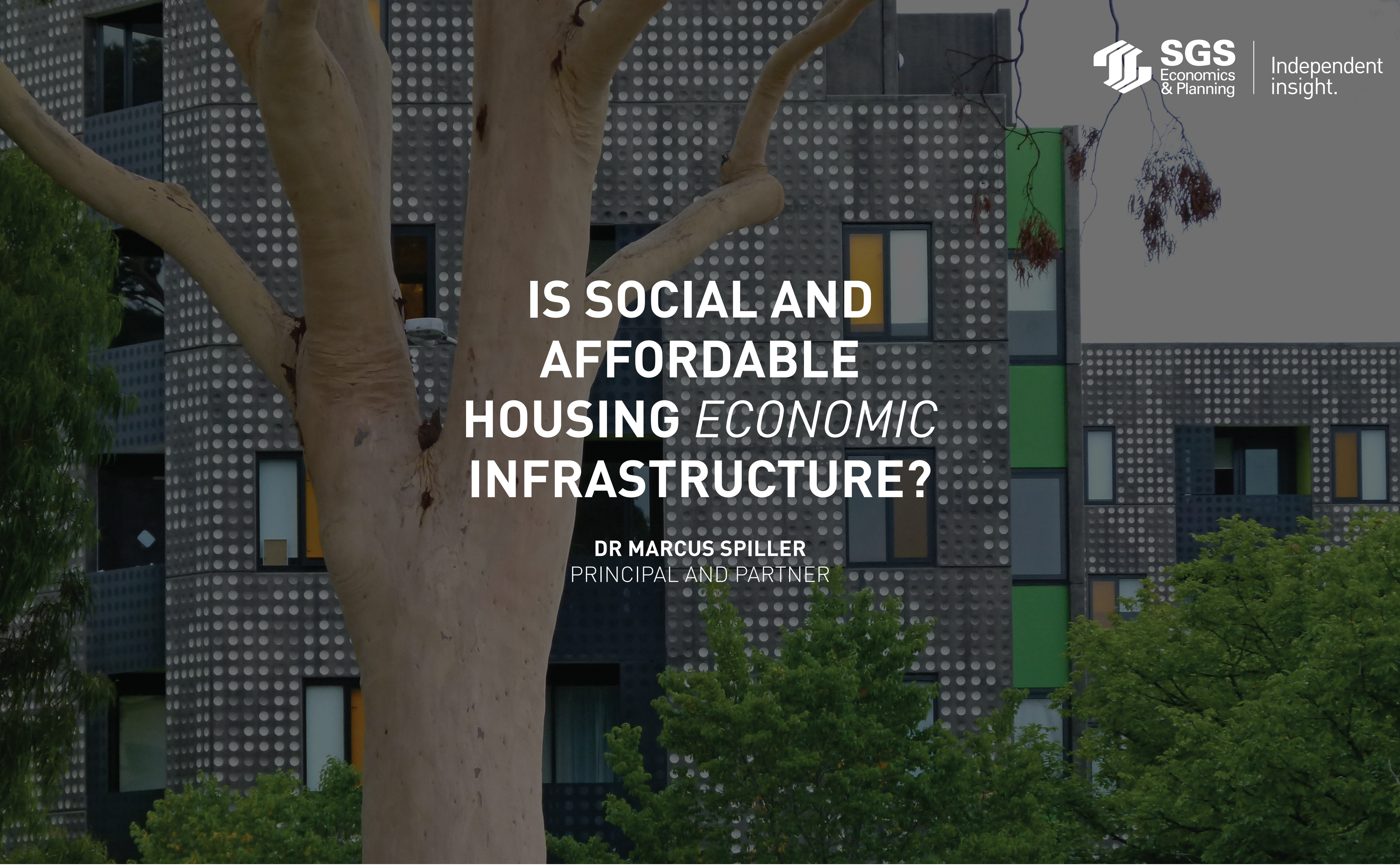

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IS SOCIAL AND AFFORDABLE HOUSING *ECONOMIC* INFRASTRUCTURE?

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IS SOCIAL AND AFFORDABLE HOUSING *ECONOMIC* INFRASTRUCTURE?

Should social and affordable housing be treated as economic infrastructure? This is more than a rhetorical question. Construing social and affordable housing (that is, secure rental housing available at around 30% of gross income for households in the bottom 40% of the income distribution) as economic infrastructure situates this issue in the realm of growing the national income pie. Meanwhile, if we see providing social and affordable housing as a welfare program its implied validation rests on redistribution – sharing the pie.

For about 5 decades after World War 2, providing social and affordable housing was seen by successive governments as economic infrastructure first. Massive public housing estates were built under the Commonwealth State Housing Agreement (CSHA) to secure a nearby supply of workers for the budding suburban car industry, the inner city manufacturing belts and busy commodity exporting ports.

In the early 1980s, social housing commencements were between 14,000 and 16,000 per year, accounting for 10% to 15% of all starts.

Through the remainder of that decade, social housing policy morphed from an economic infrastructure to a welfare discourse. New public housing starts dwindled to a trickle, interrupted only by a brief spurt of investment in 2009 and 2010 as the Commonwealth sought to mitigate the backwash from the Global Financial Crisis.

Current Commonwealth funding levels can barely sustain annual social housing starts of 2,600, particularly given the heavy cost of maintenance and replacement in the historic stock of social housing. Today, social housing represents less than 5% of all dwellings and this rate is shrinking relentlessly.

Foundation ideas in micro-economics support the case for treating social and affordable housing as economic infrastructure.

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'Infrastructure' is distinguished from other goods and services in the market by at least one of three features.

Firstly, it may be prone to 'natural monopoly'; that is, the market is only big enough to support a small number of suppliers leading to abuse of pricing power and poor quality of services. Secondly, it may involve supply which is 'non-excludable'; that is, producers cannot easily isolate consumers and extract a price for the service in question, as is typically the case with urban parklands for example. Thirdly, it supports value creation or benefit capture by third parties; while direct users of infrastructure derive a consumption benefit they simultaneously generate a welfare gain by non-users.

If any one of these conditions hold, mainstream economic theory tells us that a market operating on its own devices cannot be relied upon to deliver the optimal quantity and quality of the good or service in question. Theory indicates that Governments need to intervene, either fill the supply gap directly, or induce additional supply through regulation or subsidy.

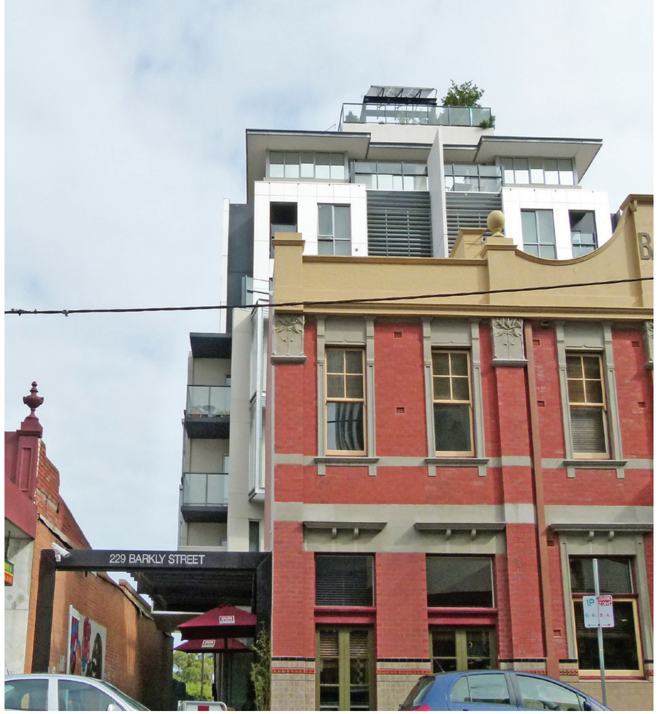
Social and affordable housing is characterised by the third of the above parameters - the creation of substantial third party benefits or 'positive externalities'.

One of the main ways it does this is by supporting labour supply for the development of firms. An historical example is provided by State and Commonwealth Government investment in Melbourne's Broadmeadows public housing estate in the 1950s and 60s as part of an effective partnership deal with Ford Motor Company which opened a plant next door.

A contemporary example is provided by the Defence Housing Authority (DHA) which brings together the rental subsidy entitlements of defence personnel with 'mum and dad' capital to ensure there is an adequate supply of affordable and appropriate rental housing wherever these personnel are posted.

The DHA, like the Ford Motor Company, cannot rely on the private rental market to meet the housing needs of its workers. This is not surprising. Whether the defence sector operates effectively or not, or whether the erstwhile car industry could secure an appropriate supply of workers, is of no material interest to investors in rental housing. All they are concerned about is the financial performance of their investment. The 'external' benefits in having particular industry sectors function properly don't figure in the investor's equation and must be paid for by the community at large, through government subsidies of one sort or another.

So, the market left to its own devices will most likely fail to deliver sufficient affordable rental housing to meet the needs of industry. The rent which is affordable to a worker on the national average salary would be around $25,000 per year. After allowing for rental operating costs, this income stream capitalises at $320,000. That won't buy an apartment in most jobs rich metropolitan suburbs.



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If we want to have affordable rental housing for workers in these areas to support industry development, then Government needs to bridge the 'return gap'.

It can do this by directly topping up returns to investors – as per the now defunct National Rental Affordability Scheme – which provided an annual subsidy of about $12,000 to landlords, or it can pursue an 'old school' solution – build and own the housing itself (or via community housing providers) and absorb the loss on the investment yield.

The reason for taking this reduction in investment yield is that it would be more than compensated by the lift in productivity in the wider economy enabled by the supply of affordable rental housing. This is a classic case of 'non-financial' government investment in infrastructure to enable income and benefit creation by third parties.

How do workers cope in the absence of a supply of affordable rental housing? They can use housing more intensively (crowd into apartments) and/or move to cheaper locations. Both strategies are likely to have adverse consequences for productivity.

AHURI estimates that around 1.3 million households Australia wide are in rental stress. For the sake of illustration, let's assume that these households account for a million workers. If their adverse housing circumstances trims 10% from their annual earnings, the reduction in the national pool of human capital would be in excess of $150 billion. This does not account for workers pushed to outboard locations where cheaper rents might be found but where there is a corresponding shrinkage of learning opportunities, either through formal courses or churn in the labour market.

To the extent that business cases for investment in social and affordable housing have been made since the 1980s, they have tended to rely on an avoided cost argument. That is, provision of 'safety net' housing might forestall or mitigate heavier social expenditures in the health and criminal justice systems.

Poviding social and affordable housing is, indeed, a prudent investment in social security. However, we ought to remember that this investment is also vital infrastructure for improved productivity and a growing national income cake.

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