

March 2020



MINISTRY OF HOUSING
AND URBAN DEVELOPMENT

Public Housing Funding Review 2019

New Zealand Government

The Public Housing Funding review has drawn on information from Community Housing Providers, Kāinga Ora – Homes and Communities, and other government agencies to assess delivery costs, government expenditure and value.

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Glossary and terminology (1 of 2)

AMS	Asset Management Strategy	IROI	Incremental return on investment
BR	Bedroom	IRR	Income-related rent
CAGR	Compound annual growth rate	(Project-/Equity-) IRR	Internal rate of return (related to project or equity)
CG	Community Group	IRRS	Income-related rent subsidy
CGH	Community Group Housing	KPI	Key Performance Indicator
CHA	Community Housing Aotearoa	LTIP	Long-term Investment Plan
CHP	Community Housing Provider	MBIE	Ministry of Business Innovation and Employment
CHRA	Community Housing Regulatory Authority	MSD	Ministry of Social Development
EBITDA	Earnings before interest, taxes, depreciation and amortisation	NPV	Net present value
EHSNG	Emergency Housing Special Needs Grant	OS	Operating Supplement
FPDG	Funding and Programme Delivery Group (at HUD)	PH	Public Housing
FY	Fiscal Year/ Financial Year (e.g. FY17 is 2016/17)	SHRP	Social Housing Reform Program
FTE	Full Time Equivalent	SHU	Social Housing Unit
HF	Housing First	RONZ	Rest of New Zealand
HIF	Housing Innovation Fund	TH	Transitional Housing
HNZ	Housing New Zealand	TM	Tenancy management
HUD	Ministry of Housing and Urban Development	UF	Upfront Funding
ICR	Interest Coverage Ratio	WACC	Weighted average cost of capital
		YTD	Year to Date

Glossary and terminology (2 of 2)

The following tables set out definitions for common terms used throughout the report.

Public Housing procurement methods

Build	Provider enters into a contract with a construction sub-contractor
Turn-key (off the plans new build)	Provider enters into a fixed price contract with a property developer for a property that has never been lived in
Buy-in (existing)	Provider purchases an existing property from the market
Build to lease	Provider enters into a long-term lease arrangement with a developer for a new build property
Redevelopment	Provider redevelops an existing property within its portfolio, usually with intensification
Lease	Provider enters into a lease arrangement with a private landlord
Redirect	Redirect is a catch-all term for Public Housing supply that hasn't come through HUD's new supply programme. These are predominately provided by CHPs through lease arrangements with private landlords, but may also include properties made available from existing CHP stock (e.g. donated, purchased, building no longer required for wider mission of the CHP, properties funded through the SHU).
Direct leasing	HUD enters into a development and lease arrangement with a property developer for a property that is then made available to a Provider to sub-lease. The developer receives a market rent during the lease term, while the Provider receives a services payment to cover its tenancy management costs. It is intended that the sum of these payments is approximately equal to a similar standard lease arrangement.

Public Housing management

Tenancy management	Activities including allocation of a tenant to a property, tenancy induction and tenancy agreement administration, rent collection, inspections, interactions with tenants to support the sustainability of their tenancy, and linking and/or providing tenants with broader social support services
Responsive maintenance	Property maintenance that is reactive day to day repairs and maintenance that is carried out on property in response to requests (e.g. from the tenant) for such work.
Planned maintenance	Property maintenance that is planned in advance, including on a cyclical basis (e.g. house painting) and preventative maintenance
Capital replacement	Activities to replace or refurbish components of the property, such as a roof replacement.

Executive summary (1 of 4)

Key points	Description	Comments/next steps
<p>There are multiple drivers to the variability in development and acquisition costs of new Public Housing supply. The data sample is too limited to draw robust conclusions between CHP and HNZ development costs and between procurement types.</p>	<ul style="list-style-type: none"> New supply of Public Housing over the last three years has varied greatly in cost per dwelling. The wide variety of property developments (scale, location, building style, land quality etc.), limited data and provider operating models means it is difficult to draw common themes. 	<ul style="list-style-type: none"> We cannot conclude on the current data whether one model of delivery is more efficient than another. However, the work highlights the importance of maintaining a team with strong capability in property development/purchase decisions to assess whether a specific development is good value given its characteristics. Further, HUD may wish to continue to consider further options for allowing more detailed data analysis of actual construction and acquisition costs given the multiple drivers of the cost of a development e.g. ground condition, style of building etc.
<p>Both HNZ and CHPs have been bringing on new Public Housing supply over the last three years, although significant new build developments are a relatively recent phenomenon for CHPs.</p>	<ul style="list-style-type: none"> Over the last three years CHPs have brought on 2,115 new dwellings (excluding the Tauranga and Tamaki transfers), of which 86% were redirects. There is a further pipeline of future CHP new supply properties supported by OS and UF. HNZ has brought on approximately 1,303 additional units, including lease renewals. Around half of new supply (excl. leases) has been through redevelopment and intensification of existing sites, with the remainder provided through turn-key and buy-in properties. 	<ul style="list-style-type: none"> HNZ has a more established track record in property development than CHPs, although CHPs are in the process of building capability in this space (or developing partnerships with parties that have capability). A policy decision is needed on whether the system wants to continue building CHP capability in this area.
<p>On average, CHPs record lower tenancy management and maintenance costs than HNZ, but key data gaps remain which make it difficult to draw conclusions of relative efficiency</p>	<ul style="list-style-type: none"> At a high-level, average tenancy management for CHPs was \$2,236 per unit, relative to \$2,929 per unit for HNZ. However, the operating models and service levels between CHPs and HNZ are significantly different and not sufficiently captured by available data. 	<ul style="list-style-type: none"> While this report provides initial analysis of available information, the data is not sufficiently detailed, reliable or comparable to draw robust conclusions on efficiency across different parts of the sector, including controlling for tenant cohort, service levels and property characteristics.
<p>The total cost, including cost of capital, of delivering new Public Housing exceeds market rent</p>	<ul style="list-style-type: none"> Market rent alone appears insufficient to cover operating costs and a cost of capital for new supply units of Public Housing, given the return requirements for both CHPs and HNZ. This is likely due to relatively low rental yields in a market where private developers achieve their target total return through assumed capital gains. Further, for the CHP sector, market rent is constrained by the current rental maxima set in 2016 and may not represent a true market rent. 	<ul style="list-style-type: none"> The insufficiency of market rent to cover the costs of new supply provides justification for additional funding tools to enable new supply. Any funding approach designed to facilitate CHP property developments, needs to recognise the cost of capital faced by CHPs to ensure sufficient capital is attracted to the projects.

Executive summary (2 of 4)

Key points	Description	Comments/next steps
<p>Total IRRS expenditure is driven by changes in volume, market rent and the typology mix of CHP and HNZ portfolios</p>	<ul style="list-style-type: none"> The increasing IRRS per place has been driven by increasing market rents over the period, particularly in growth regions. However, based on indicative analysis, there is not clear evidence that Public Housing rent movements have been inconsistent with the general market. Total IRRS expenditure is also impacted marginally by OS payments in the CHP sector. This is difficult to accurately separate from IRRS expenditure as it is a single appropriation. 	<ul style="list-style-type: none"> As discussed further in section 6, we see merit in HUD further considering market rent settings in Public Housing. As the key cost driver for government, there should ideally be transparency, consistency and sufficient monitoring across the sector in how rents are set.
<p>Upfront Funding (UF) and Operating Supplement (OS) have indicatively had a broadly similar cost per unit for developments approved to date, although are not calculated on the same basis</p>	<ul style="list-style-type: none"> OS provides an operating subsidy for new supply units, provided as a percentage top-up on market rent. UF provides an upfront payment, but is no longer generally available for new developments due to funding constraints. UF supported 27 developments and OS supported 39 developments. Both funding tools mostly supported the development of 1 and 2 bedroom units. UF ranged from \$95k to \$290k per unit, with an average of \$196k. OS on average was \$155k for 1 bedroom and \$194k for 2 bedroom units. 	<ul style="list-style-type: none"> There is nothing inherent in the design of an operating subsidy or an upfront payment that necessitates either form of subsidy being more costly to the Crown. As set out in section 6, we see benefit in both funding tools being available to enable new supply.
<p>While HNZ has comparatively detailed cost and performance reporting, the relative performance of the CHP sector is difficult to determine from a data perspective due to a lack of robust information</p>	<ul style="list-style-type: none"> The value for money framework adopted in this report considers performance against three types of metrics: <ul style="list-style-type: none"> Economy: input costs Efficiency: spend to outputs Effectiveness: achieving desired outcomes The metrics considered in the framework are typical for assessing value within public and social housing systems internationally. The value for money analysis suggests that HNZ's performance is broadly in line with expected benchmarks, although there are still data limitations. HNZ uses performance data for internal management, some of which was made available to us in this review. The performance of the CHP sector is challenging to convey with data. There is only limited consolidated data held by government agencies, although we sought to complement this with results from a survey. 	<ul style="list-style-type: none"> A key potential benefit from a diverse CHP sector is the specialisation of tenancy management from smaller local organisations that have experience in meeting the needs of particular tenant cohorts. However, this is still mostly only evidenced through limited qualitative information, rather than data. The new contracting framework for CHPs represents a step forward in the collection of performance information on the sector, as this not currently collected in a systematic way across the sector. We consider there is still significant scope to further improve cost and performance benchmarking across Public Housing in line with other jurisdictions, as set out in section 5.

Executive summary (3 of 4)

Key points	Description	Comments/next steps
<p>Current data limitations do not allow robust cost benchmarking across Public Housing, and New Zealand appears to lag behind both the UK and Australia in this area</p>	<ul style="list-style-type: none"> Benchmarking is the practice of comparing cost and performance metrics against peer local organisations, international standards, comparable programmes or specific targets. The potential benefits of effective benchmarking include being able to consistently assess relative costs and outputs, provide a signal to providers on performance expected by the purchasing agency and provide data and tools to providers to identify improvement opportunities. There are international examples in the UK and Australia on approaches to conducting benchmarking that seek to control for factors that may drive legitimate cost differences between providers. 	<ul style="list-style-type: none"> HUD currently undertakes some benchmarking of costs as part of the Gateway 2 process for evaluating new supply proposals. There is, however, no existing benchmarking framework for Public Housing as a whole, and data limitations mean that any indicative results are open to the critique that legitimate cost drivers are not adequately controlled for. We see merit in HUD developing a benchmarking framework for Public Housing, including the identification of key benchmark metrics and associated data collection guidance (e.g. break-down of tenancy service levels, overhead cost allocation, tenant information collection methodologies). The level of detail in benchmarking needs be balanced against the administrative burden on both HUD and providers.
<p>We identified five areas within existing Public Housing funding settings that HUD may wish to consider further through its policy process</p>	<ul style="list-style-type: none"> The five broad areas are focused on: <ul style="list-style-type: none"> tools to incentivise and enable new Public Housing supply market rent setting the setting and administration of the OS data and performance information financial performance regimes 	<ul style="list-style-type: none"> HUD may wish to consider further short-medium term policy work in the areas identified. Based on our initial thinking, we see merit in: <ul style="list-style-type: none"> a broad range of funding tools to incentivise new supply a review of the differential approach to market rent setting in different parts of the sector ensuring transparency in the calculation and reporting of OS consideration of further data collection, and potentially in the medium term, financial incentives for performance.
<p>Further consideration could be given to a cost-based approach to funding providers, but this would represent a fundamental shift in the existing legislative and policy paradigm</p>	<ul style="list-style-type: none"> The current funding approach is fundamentally based on the payment of a market rent (albeit constrained by the maxima policy for CHPs) to providers as managers of properties, similar to a regular landlord. This approach has limitations which are already evident in the need for OS and UF for new supply. Further, the existing approach provides limited transparency and control of costs for HUD. There are a number of potential alternative 'rent' setting methods, including setting income for providers on the basis of a formula, a cost stack or other approaches not related to cost of delivery. 	<ul style="list-style-type: none"> While we have not undertaken an in-depth review of alternative models as part of this report, we do see merit in HUD exploring in the medium-term whether alternative models would improve transparency and financial certainty for the Crown.

Executive summary (4 of 4)

Key points	Description	Comments/next steps
<p>Housing First (HF) provides a wrap-around support intervention for a vulnerable cohort</p>	<ul style="list-style-type: none"> The available data suggests that costs for each HF placement and support (over two years) are broadly similar between providers (approximately \$30,000 over two years). Accommodation support costs (mostly IRRS) are on top of this. HF providers are required to submit performance information to HUD on HF cohort information and status (i.e. housed, still in programme). The quality of this data is mixed, but HUD is taking steps to improve its reliability. 	<ul style="list-style-type: none"> HUD should continue to collect and improve the reliability and scope of data to measure performance as the programme matures. HUD should consider the key metrics and framework that it wishes to use to monitor the performance of HF providers over time, including broader tenant wellbeing measures.
<p>Transitional Housing (TH) has pursued a supply based approach as a priority which has resulted in relatively high accommodation costs through contracted motel provision</p>	<ul style="list-style-type: none"> The ramp-up of TH has been through a supply-based strategy where HUD has primarily sought to increase the number of units in the programme, including through extensive use of contracted motel units. There is not clear visibility of the different service models used by TH providers. Further, the available performance data is considered mixed quality and therefore it is challenging to measure comparative performance and outcomes. 	<ul style="list-style-type: none"> HUD should continue to collect and improve the reliability and scope of data to measure performance as the programme matures, including a view of the future demand for places.
<p>Community Group Housing (CGH) provides community groups with accommodation support, but current funding arrangements do not provide clear cost transparency.</p>	<ul style="list-style-type: none"> CGH provides support to community groups to deliver their services to their target clients, particularly where the provision of that service requires residential housing. This support is provided through concessionary rent arrangements and further rent subsidies. In addition, community groups can benefit from bespoke properties that are acquired and appropriately modified through the programme. 	<ul style="list-style-type: none"> The existing settings do not provide clear transparency and accountability of the full cost of funding services to support tenants in CGH. There are multiple subsidy streams across multiple agencies. We are supportive of HNZ's current work to improve existing CGH arrangements by improving consistency across providers and seeking to align funding with responsible agencies.

Summary across subsidised housing programmes (1 of 2)

	Public Housing	Housing First	Transitional Housing	Community Group Housing
Description and target cohort	Subsidised medium-long term housing for those that have a serious housing need that is not being met by the private market.	Immediate and unconditional housing for those who have been homeless for a long time or have multiple complex needs, with intensive wrap-around support services.	Temporary housing for those that do not have anywhere to live and have an urgent need for a place to stay, with additional support service component.	Support for Community Groups to deliver their services to their target client, particularly where the provision of that service requires residential housing.
Funding settings	Tenants generally pay up to 25% of their income towards the rent (IRR), with the remainder subsidised by government (IRRS). Additional funding for new supply (currently OS) also available. UF is still available in limited circumstances and is continuing to support new supply by CHPs.	Public Housing IRRS funding settings apply for those HF clients in Public Housing. A small proportion of HF clients as in market housing supported by AS. Wrap-around services are funded to providers on the basis of anticipated number of client engagements.	Tenants generally pay up to 25% their income towards the rent (similar to IRR), with the remainder subsidised by government.	Rent can be subsidised through two mechanisms – a concessionary rent arrangement with HNZ and a further subsidy to support the CG to meet the concessionary rent.
Separate tenant support component	No. Any tenancy management is covered within the market rent received by Public Housing providers.	Yes. HF service component is separately costed and paid to HF providers.	Yes. TH service component is separately costed and paid to TH provider in addition to accommodation subsidy.	Yes, but not via the CGH programme directly. Services provided by CGs to support their clients are funded by other government agencies (e.g. Ministry of Health).
Indicative government subsidy cost per place per annum	<ul style="list-style-type: none"> IRRS: \$15k per place (approximately 70% of market rent). This incorporates a small portion of OS. 	<ul style="list-style-type: none"> IRRS: Approximately \$15k per place (same as Public Housing). HF service component: <ul style="list-style-type: none"> - New client: \$15k. - High intensity existing client: \$27k. - Medium intensity existing client: \$17k. - Low intensity existing client: \$13k. 	<ul style="list-style-type: none"> TH accommodation component: \$13.2k (long-term) to \$54k (motels) per place. TH service component: \$18k per place. 	<ul style="list-style-type: none"> CGH concessionary rent: 40% of market rent. CGH rent support subsidy: 11% of market rent.

Summary across subsidised housing programmes (2 of 2)

	Public Housing	Housing First	Transitional Housing	Community Group Housing
<p>Relative value and trade-offs between housing programmes</p>	<p>While this report considers the cost and value of four government subsidised housing programmes, the programmes are fundamentally different. This means that direct trade-offs between programmes and relative value judgements are challenging. In particular:</p> <ul style="list-style-type: none"> — The programmes do not represent alternative interventions for a similar cohort seeking to achieve a similar set of objectives. For example, the objectives and purpose of Public Housing (primarily supporting those who cannot access accommodation in the private market) are significantly different to those of Housing First (supporting long-term homeless to reduce harmful factors influencing accommodation sustainability and overall wellbeing). — The benchmark standards and service levels across the programmes are not consistent. Within the framework of value for money analysis, it is difficult to find similar and genuinely comparable metrics that span across programmes. This is challenging even within each programme, where factors such as tenant cohort can be the potential driver of differential results between providers, but data is not sufficient to adequately control for such factors. — Funding arrangements differ significantly. For example, a Housing First client is also, in most cases, a Public Housing tenant and therefore the cost of subsidised accommodation between a HF client and a Public Housing tenant is therefore the same. However, a HF client also receives an additional set of wrap-around services funded separately, and for which there is nothing comparable for a standard Public Housing tenant. Similarly, CGH funding arrangements are based on negotiated arrangements with community groups and have no reference to the circumstances of the eventual tenants. <p>In general, value for money analysis does not seek to provide a view of total net social and economic benefit of different policy interventions. For example, it does not look to answer whether broader cost savings and wider social benefits of reducing homelessness outweigh the cost of a particular government intervention. Economic cost benefit analysis (CBA) does seek to consider this type of analytical question (by quantifying all benefits into monetary terms, where possible), but is generally less practical in identifying performance issues and monitoring progress of policy interventions.</p> <p>Trade-off questions/framework</p> <p>In a situation where government is seeking to consider its relative investment choice between the existing programmes and/or potentially further incremental investment in a programme, the following basic criteria may act as a guide to assist decision making:</p> <ol style="list-style-type: none"> 1. Is there a clear understanding of the characteristics of the target cohort for each programme? (i.e. clear evidence of a particular type of cohort that requires support) 2. Is there a clear understanding of the level of current and future unmet demand within a programme in serving the target cohort, such as through a specific waitlist or other social data indicating an unmet need. 3. Are there current or future proposed mechanisms to monitor the effectiveness of additional investment? 			

1

Background

Background

Introduction and scope

HUD has commissioned KPMG to undertake an independent review of subsidised housing expenditure including Public Housing, Transitional Housing, Housing First and Community Group Housing.

Introduction

The Ministry of Housing and Urban Development (HUD) was established in 2018 to consolidate the provision of advice regarding housing and urban development. It brought together functions that were previously situated in the Ministry of Business Innovation and Employment (MBIE), Ministry of Social Development (MSD) and the Treasury. At a high-level, the government's housing programme is focused on:

- ending homelessness.
- making room for growth in New Zealand's urban centres.
- helping create thriving communities.

As part of meeting these objectives, HUD provides strategic advice to government on its subsidised housing programmes. To inform this advice on policy and funding settings, HUD has commissioned KPMG to undertake a review of costs and government expenditure. For the purposes of this review, these programmes consist of:

- **Public Housing** – medium to long-term subsidised housing provided by Housing New Zealand (HNZ) or a registered Community Housing Provider (CHP)*, where tenants pay an income-related rent.
- **Transitional Housing (TH)** – temporary housing provided for an average of 12 weeks or more for those who have an immediate housing need.
- **Housing First (HF)** – a programme to support the long-term homeless and/or those with complex needs.
- **Community Group Housing (CGH)** – a programme that supports Community Groups (CGs) to provide services to their target cohorts by providing subsidised accommodation to the CG.

The largest of these programmes is Public Housing, which therefore forms the bulk of the focus of our review.

Scope and purpose of this review

The scope of our review is to discuss the costs, government expenditure and value in the delivery of the government's subsidised housing programmes.

A summary of the key outputs of the review, as set out in our CSO, are as follows:

- Develop a value framework for assessing the relative costs and benefits of subsidised housing programmes.
- Gather information on the cost of providing subsidised housing by typology, provider, region and procurement type.
- Provide a breakdown of asset and property development costs, on-going maintenance and tenancy management costs.
- Provide analysis of recent government expenditure and an assessment of value for money.
- Provide an analysis of the costs to maintain/reconfigure existing stock and the trade-offs that need to be made in terms of bringing on new supply
- Provide an analysis and discussion of broader relative costs and benefits of HNZ and CHP delivery of Public Housing.
- Provide a discussion of the constraints and risks in delivering subsidised housing under current policy settings.
- Provide an indication of possible independent benchmarks that could be set for Public Housing.
- Discuss potential areas of funding reform.

* A CHP must be registered with the Community Housing Regulatory Authority (CHRA) in order to provide Public Housing. All references to CHPs undertaking Public Housing therefore refers to registered CHPs.

Background

Structure and information sources of this report

We have structured our report into 10 sections covering the scope of the review.

Our report is primarily based on information provided by HUD, HNZ, MSD and a survey of the CHP sector.

Structure

Our report is structured as follows:

1. Introduction

This section.

2. Costs of delivering new supply of Public Housing

An analysis of available information on the development and operational costs of the delivery of new supply public housing by HNZ and CHPs.

3. Public Housing government expenditure and value for money

An analysis of recent government expenditure on Public Housing and a discussion of performance against key value for money metrics.

4. HNZ's stock reconfiguration and maintenance plans

A brief commentary on HNZ's recent draft of its LTIP and Asset Management Plan. These plans were being updated during our review, and as such, we only provide a high-level summary based on information made available to us.

5. Public Housing Benchmarking

An analysis of the challenges in undertaking cost and quality benchmarking in Public Housing, international approaches, potential metrics and next steps.

6. Constraints and risks of current Public Housing funding settings

A commentary of the key constraints and risks of current funding settings in the cost-effective delivery of Public Housing.

7. Potential areas for future funding reform in Public Housing

A discussion of potential areas for future reform of funding settings for Public Housing.

8. Housing First

A summary of the costs of delivering Housing First and preliminary performance and value for money information.

9. Transitional Housing

A summary of the costs of delivering Transitional Housing and summary of available performance and value for money information.

10. Community Group Housing

A summary of the costs of delivering Community Group Housing and available performance and value for money information.

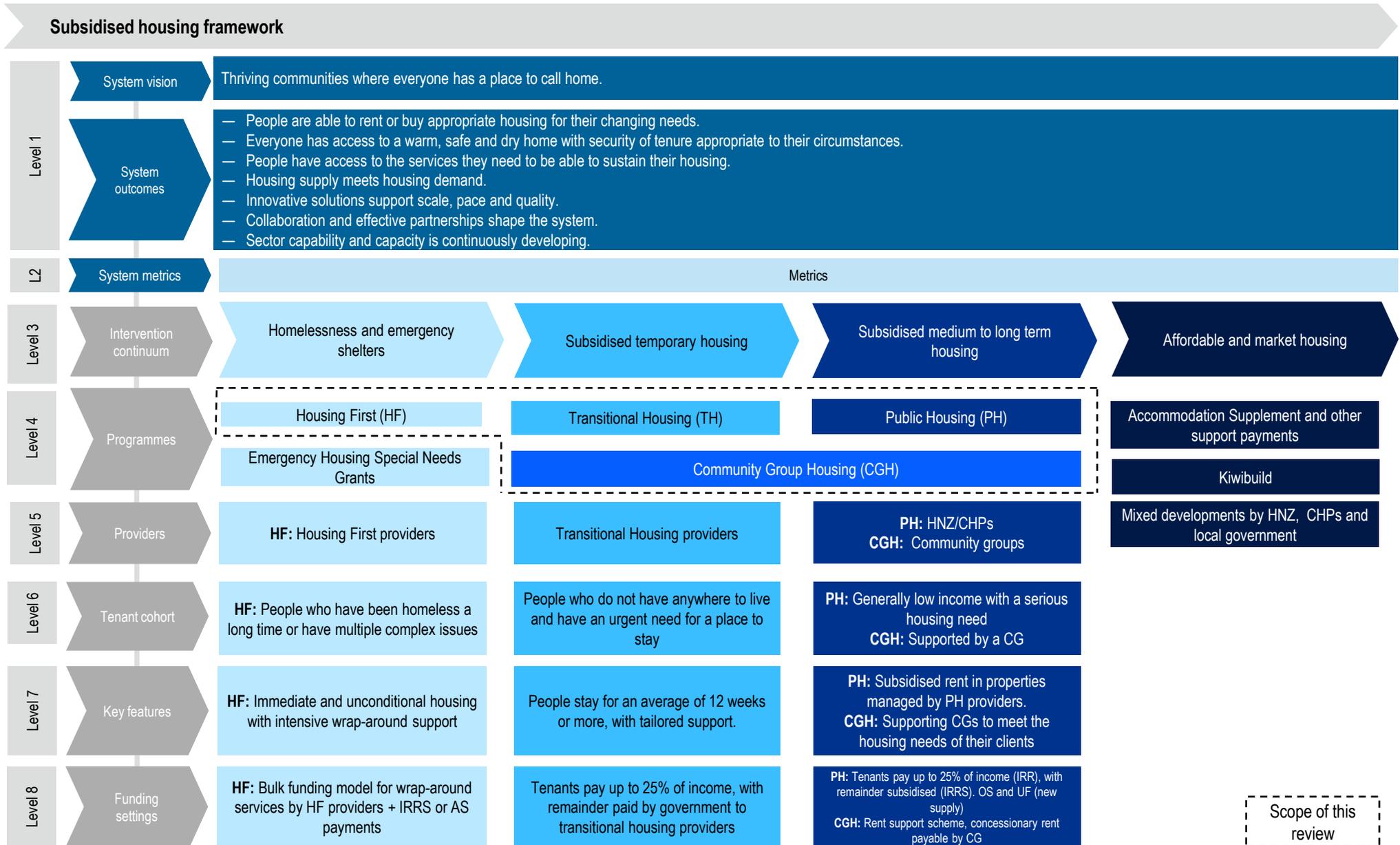
Key Information sources

Our key information sources for this work are as follows:

- Costs associated with the delivery of new supply provided by the HUD Funding Programme and Delivery Group (FPDG) for the CHP sector and by HNZ for its own properties.
- Performance metric data and qualitative information for the CHP sector from a survey undertaken by HUD and Community Housing Aotearoa (CHA).
- Performance metric data for HNZ provided by HNZ.
- Government expenditure data provided by MSD and HUD.
- CHP housing portfolio information based on the Supply Survey conducted by CHA.
- Housing First and Transitional Housing data provided by HUD.
- Community Group Housing data provided by HNZ.

Background

Subsidised housing landscape



2

Costs of delivering new Public
Housing supply

Costs of delivering new Public Housing supply

Background

Public Housing provides subsidised housing to those who have a serious housing need that is not being met by the private market.

The vast majority of properties (broadly 90%) are provided by HNZ.

Introduction and scope of this section

This section primarily focuses on the development and operational costs of new Public Housing supplied by HNZ and CHPs, with consideration of regional, typology and procurement type differences. In particular, the analysis is focused on the costs incurred by the provider in delivering Public Housing, rather than government expenditure (discussed further in section 3).

Background

Public Housing provides subsidised housing support for those that have a serious housing need that is not being met by the private market. The allocation of tenants is managed by MSD through the Public Housing Register. The Public Housing Register is the list of tenants that are eligible for a public house but have yet to be allocated a property.

The key eligibility criteria for accessing Public Housing are:

- be aged 16 years and over.
- meet the income and asset tests.
- have a serious and immediate housing need.
- be ordinarily resident in New Zealand, and be a New Zealand citizen or permanent resident.

When a prospective tenant is assessed to meet the above eligibility criteria, the tenant is added to the Public Housing Register. This works on a priority basis with the length of time until placement being guided by the tenant's housing urgency, available properties and particular housing needs. Given there is currently no demand forecasting tool, the Public Housing Register currently acts as a key means for HUD to gauge demand.

Note: Market rent is defined in the Housing Restructuring and Tenancy Matters Act 1992 as the rent for the time being determined by the provider or the Tenancy Tribunal as the market rent for that housing. For CHPs in particular, where market rent is referenced in this report, this refers to the determined rent which is subject to the rental maxima policy, rather than the 'true' market rent for the property (unless stated otherwise).

Role of the provider

Public Housing is provided by either HNZ or 48 registered CHPs. The role of a provider is to acquire or lease the Public Housing property, manage the relationship with the tenant (e.g. tenancy agreement administration, rent collection, inspections) and maintain the property. In addition, many providers provide additional services (over and above typical landlord obligations) to support the well-being of their tenants.

Role of the tenant

As a Public Housing tenant, the tenant must meet typical tenancy obligations, such as timely payment of rent and care of the property that is being rented. Tenants are not obliged to engage with wider services offered by the provider.

Rent setting

The total income that a Public Housing provider receives for a tenancy is based on the market rent for the property, with the respective processes for HNZ and CHPs set out below.

HNZ

HNZ updates market rents quarterly using a two stage process. The first stage is to review local benchmark rents against comparable private sector rents. The standard benchmark rent has 16 weighted associated property features, which are then adjusted in Stage 2 to reflect the specific characteristics of the actual individual property for which the rent is being assessed. This adjusted benchmark is the market rent for the property.

CHPs

CHPs determine a 'market rent', generally every 6-12 months, in accordance with their own policies, but must set rent levels within the region and typology rent maxima set by HUD. Where rent is set significantly above lower quartile rents, HUD references MBIE bond data supplemented with other market information (e.g. trademe rental listings) to check the reasonableness of rent levels.

Costs of delivering new Public Housing supply

Background

Revenue for Public Housing providers is based on market rent, the payment of which is split between the tenant and government.

In addition, current policy settings allow providers to apply for OS to incentivise and enable the delivery of new supply units.

Background: Funding settings

Rent income

The payment of the market rent set for a tenanted property consists of two components:

- Income Related Rent (IRR): The portion of market rent paid by the tenant, generally up to 25% of the tenant's income. This is collected directly from the tenant by the provider.
- Income Related Rent Subsidy (IRRS): The portion of market rent paid by the government, set as the difference between the determined market rent for the property and the IRR.

In addition, there are a number of further funding sources, current and historic, to incentivise the delivery of new supply units.

Operating Supplement (OS)

OS is an operating subsidy of up to 90% of market rent paid to the provider. The property must generally be a net new supply unit to the housing market. Further details on OS setting is provided in section 6.

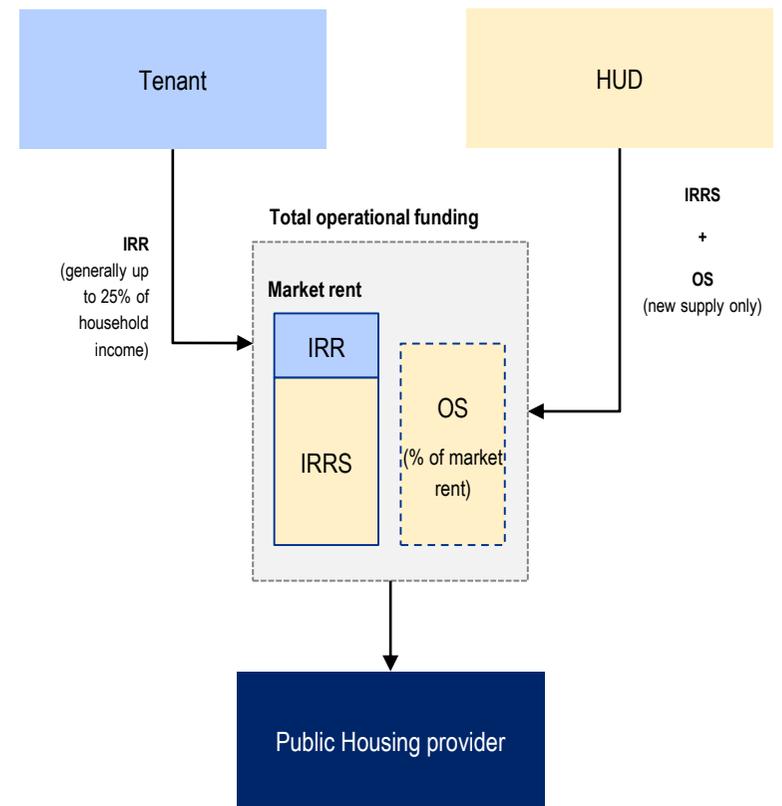
Upfront Funding (UF)

UF is an upfront prepayment of OS to CHPs to support the financial viability of a new supply proposal. UF is no longer typically available for new developments, although further UF drawdowns are anticipated for developments already approved.

Historic government support for new supply

Historically, two programmes in particular have supported the development of new Public and affordable housing by NGOs and councils through conditional capital grants and loan arrangements. Further detail on the Housing Innovation Fund (HIF) and the Social Housing Unit (SHU) Fund are provided in section 3.

Diagram: High-level funding flows



Costs of delivering new Public Housing supply

Growth in Public Housing supply

As at December 2018, there were approximately 67,000 Public Housing tenancies.

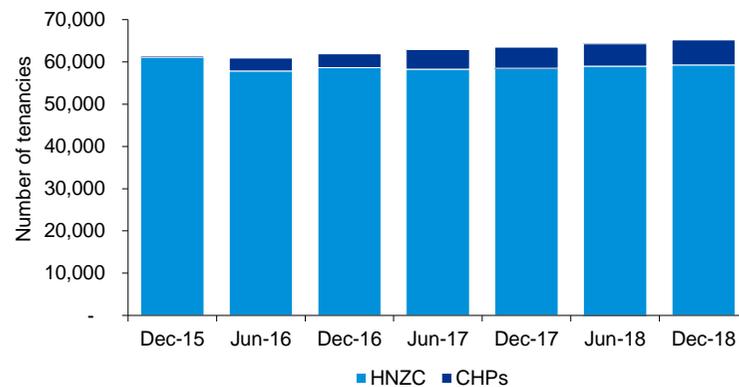
The recent growth in CHP supply has been predominately through 'redirects' of existing properties into Public Housing, including two large transfers from HNZ.

The recent growth in HNZ's portfolio has been predominately driven by turn-keys, buy-ins and redevelopments.

Movement in total Public Housing supply

The following diagram sets out changes in total Public Housing supply (tenancies qualifying for IRRS) over the last three years.

Diagram: Historic movement in IRRS properties



Source: Ministry of Social Development.

Recent CHP Public Housing supply growth

Following a policy change in 2014 to allow CHPs to receive IRRS, the number of CHP Public Housing properties has grown to approximately 6,000*. This growth has been supported by two transfers:

- The transfer of 2,800 of HNZ's properties to the Tamaki Regeneration Company (with properties to be managed by the Tamaki Housing Association) in April 2016.
- The Tauranga transfer transaction of 1,138 properties from HNZ to Accessible Properties in April 2017.

As shown, the majority of recent growth in CHP new supply has been in 'redirect' properties (often leased from the private market).

* CHPs manage approximately 13,300 in total, including non-IRRS affordable properties

Table: Recent CHP new supply (gross)

	2016/17	2017/18	2018/19	Total
Build/Turn-key	102	32	164	298
Redirect	351	676	790	1,817
Tauranga	1,138	-	-	1,138
Tamaki (Apr 16)	2,800			
TOTAL	3,938	708	954	6,053

Recent HNZ Public Housing supply growth

HNZ's recent supply growth has been predominately driven by new turn-key purchases, purchases of properties from the market and redevelopments (with intensification) of its existing properties.

Table: Recent HNZ new supply (gross)

	2016/17	2017/18	2018/19	Total
Turn-key	54	156	421	631
Buy-in	230	249	402	881
Redev.	355	682	1,040	2,077
Leases**	471	797	105	1,373
Total (excl. leases)	1,110	1,884	1,968	4,962

We have provided further detail on HNZ's net new supply (i.e. after taking account of demolitions and expired leases) in section 3.

** Leases over the previous three years have been largely lease renewals

Costs of delivering new Public Housing supply

Procurement methods for new supply

Public Housing Plan 2018-2022

HUD's Public Housing plan sets out the government's plan for delivering additional Public Housing supply. In particular, the plan sets out:

- The aim to deliver 6,400 additional public housing places by June 2022, with delivery to be split approximately 70% (HNZ) and 30% (CHP sector).
- The desire to bring on as many public housing places as possible within existing funding.
- A preference for new builds relative to leases and buy-ins.

Summary of procurement methods

There are a number of procurement options for providers to bring on additional Public Housing supply into their portfolios. **There is no single preferred procurement type in all circumstances, with each model providing a different cost and risk profile for the provider.** A summary of the typical characteristics of each model is set out below (broadly indicative only).

Diagram: Public Housing procurement model summary

Procurement methods for new supply										
Method	Description	Qualifies for OS	Upfront capital required	Timescale	Construction risk transfer	Ownership	New build/existing	Provider management burden	Bespoke design opportunity	Predominant provider
Build	Provider enters into a contract with a construction sub-contractor	Yes	Yes	Medium	Low	Provider	New build	High	High	CHPs
Turn-key (off the plans new build)	Provider enters into a fixed price contract with a property developer for a property that has never been lived in	Yes	Yes	Medium	High	Provider	New build	Medium	Medium	HNZ/CHPs
Buy-in (existing)	Provider purchases an existing property from the market	Yes (outside Auckland)	Yes	Low	N/A	Provider	Existing property	Low	Low	HNZ
Build to lease	Provider enters into a long-term lease arrangement with a developer for a new build property	Yes	No	Medium	High	Developer / investor	New build	Medium	Medium	CHPs
Redevelopment	Provider redevelops an existing property on its own land, usually with intensification	Yes (net additional)	Yes	Medium	Medium	Provider	New build	High	Medium/High	HNZ
Lease (incl. redirects)	Provider enters into a lease arrangement with a private landlord	No	No	Low	N/A	Private landlord / CHP	Existing property	Low	Low	HNZ/CHPs
Direct leasing	Provider sub-leases a property from HUD developed through a direct leasing agreement	Yes	No	Medium	N/A	Developer	New build	Low	Medium	CHPs

Costs of delivering new Public Housing supply

Scope of new supply cost data (1 of 2)

We requested cost data on recent new supply from HNZ and from the HUD FPDG (for the CHP sector).

HNZ's cost data is focused on delivered units over the previous three years.

The CHP sector's cost data is based on business case costs proposals submitted to HUD for CHPs to qualify for OS and UF (rather than actual spend incurred).

HNZ new supply cost data

HNZ provided data on new supply properties in its portfolio delivered between April 2016 to March 2019. This represents actual new supply over this period, and therefore does not include cost data on planned or new units still in development.

- The dataset includes 4,113 new supply properties delivered over the period in total. Of the 4,113 new supply units, 1,640 did not include development costs (mostly leased properties). We then sought to isolate and comment on the impact of land values on total costs. HNZ provided splits of land, property and other costs for 1,048 properties (all of which are of the turn-key or buy procurement types).
- The total development cost is based on the cost as reported in HNZ's fixed asset register.
- The dataset includes property level information, including address, typology, size, region, procurement method, and acquisition date.
- We sourced additional operational cost data from HNZ separately.

CHP new supply cost data

Our data for the prospective cost of new supply by the CHP sector is based on summary data held by HUD, submitted to HUD as part of the qualification procurement process for new supply projects to receive OS and UF. The data represents, in HUD's view, the most reliable source of available cost data for this review. In addition, we have a small number of whole of life models using the recently implemented standard CHP financial model.

- Our base dataset includes 36 developments representing 951 new places, with total capital development costs of approximately \$300m.
- The vast majority of the developments are in Auckland, limiting the scope of any potential regional analysis. This reflects that new supply funding prior to Budget 2018 was only available in Auckland.
- The dataset is almost exclusively 1 and 2 bedroom properties.

Diagram: HNZ development cost dataset

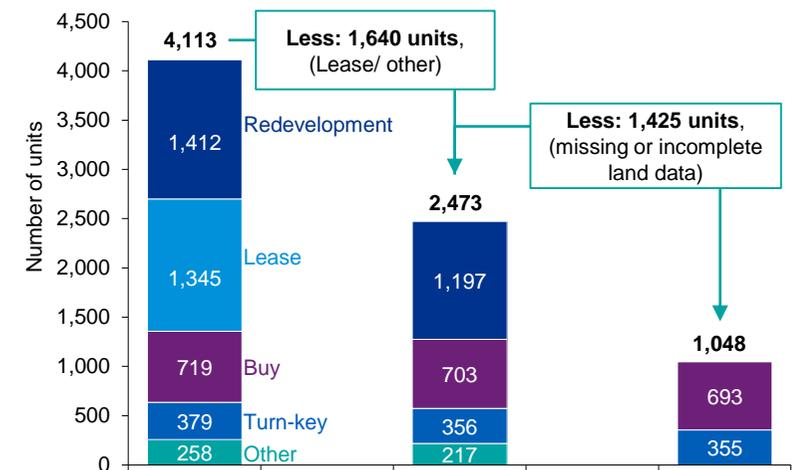


Table: CHP new supply cost data

CHPs: HUD benchmark summary						
Region	No. of CHPs	No. of developments	No. of properties	Made up of		
				1 bedroom	2 bedroom	Other
Auckland	11	27	746	446	298	2
Canterbury	1	3	40	25	15	
Tauranga	1	2	62	15	47	
Hastings	1	1	24	6	18	
Napier	1	1	10	9	1	
Palmerston North	1	1	44	18	26	
Lower Hutt	1	1	25	8	13	4
Total	17	36	951	527	418	6
<i>Made up of:</i>						
Build		12	397	267	126	4
Turn-key		11	127	30	95	2
Direct leasing		7	278	123	155	
Lease		6	149	107	42	

Costs of delivering new Public Housing supply

Development and acquisition costs

The available datasets focused on total development and acquisition costs, which limited the scope for a break-down of these components.

We note that more detailed information does generally exist embedded across individual business cases and other documents, but the manual collation of this information was outside the scope of this report.

Development and acquisition cost categories

The table below sets out the key cost categories that would generally sit within upfront development and acquisition costs (excluding GST) for each procurement type, and the data available (i.e. the extent to which the category could be separately identified) within our datasets.

Category	Description	CHP data	HNZ data
Design and Build, Turn-key, Build to Lease and Redevelopment			
Land	The value of land used in the development.		
Site Civils and Infrastructure	The cost of demolition and site works (including decontamination) and supporting infrastructure.		
Construction	The cost of building works.		
Development margin	In the case of developer-led procurements, the margin for the developer (typically in the order of 15%).		
Professional and other fees	The cost of external consultants, such as designers, surveyors and other consultants.		
Consent fees	The cost of Council and consenting fees (typically in the order of 2%).		
Total cost (including land)	The total cost of the new build (either partnering with a developer or a construction firm directly).		
Total cost (excluding land)	As above, but separately excluding the land component of the development.		
Buy-in (existing)			
Capital value	The purchase price for a buy-in property (incorporating both a land and property component). Where available, a proportional split is generally an estimate completed for financial management and accounting purposes.	Not applicable	
Land			
Redirect and Lease			
These procurement types do not have an associated development cost for the Public Housing provider.		Not applicable	Not applicable

Not available for this review

Partially available for this review

Available for this review

Costs of delivering new Public Housing supply CHP - Development and acquisition costs

Our analysis is based on a relatively limited sample of CHP developments, but indicates that the development cost in Auckland of a 1 bedroom unit for a CHP is, on average, approximately \$446,000, with a 2-bedroom being \$543,000.

We note there is a reasonably high level of variation within the data.

Key findings

Our dataset does show some cost variation in procurement types, but it is difficult to isolate the drivers of this

As noted, the relatively high-level development cost data is dominated by Auckland developments of 1 and 2 bedroom units.

Based on our dataset, we can make the following observations:

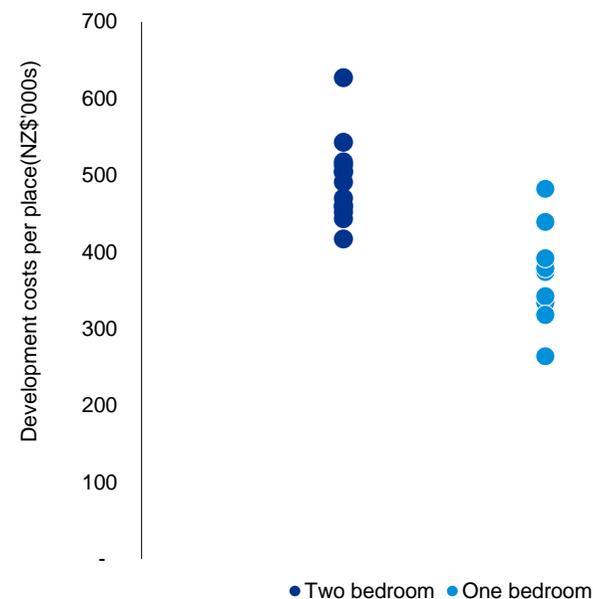
- As would be expected, there is a significant difference in development costs between Auckland and the rest of New Zealand (approximately \$92,000 on average). We have not attempted to break-down the rest of New Zealand due to the small sample size.
- After controlling for typology, there is not a significant difference between the Build and Turn-key procurement types in Auckland, although Build costs are marginally higher in this dataset. We caution against drawing broad conclusions given the small sample and potential for project-specific characteristics to be driving this.

Table: Average development cost per place

CHPs: Average development costs		
NZ\$'000s	One bedroom	Two bedroom
Auckland		
Build	479	592
Turn-key	419	565
Direct leasing	335	442
Total - Auckland	446	543
Rest of New Zealand		
Build	251	333
Turn-key	276	422
Direct leasing	269	343
Total - Rest of New Zealand	262	355
New Zealand		
Build	436	488
Turn-key	376	533
Direct leasing	300	377
Total - New Zealand	393	460

- We note that the 'direct leasing' model appears lower cost than either Build or Turn-key in Auckland, although the sample size is too small on which to draw any conclusions. In these cases, the development is undertaken by a private developers with the key contractual agreement sitting between HUD and a private developer. On completion, the property is leased back to HUD, which then sub-leases the property to a CHP. Our data does not allow us to draw conclusions on the driver of this difference, such as site specific issues, quality or developer efficiency.

Diagram: Spread of development costs per unit in Auckland



Costs of delivering new Public Housing supply HNZ - Development and acquisition costs (1 of 2)

Our HNZ cost analysis is based on actual costs incurred over the last three years.

Similar to the CHP sector, the analysis confirms the significant cost difference between Auckland and the rest of New Zealand.

Key findings

Our data provides the total development costs for new units across the turn-key, buy-in (existing properties) and redevelopment procurement types.

Based on our dataset, we can make the following observations:

- As expected, there is a significant difference in the cost of developments in Auckland relative to the rest of New Zealand
- After controlling for typology, there is not a consistent difference in the cost between Turn-key and existing property purchases, suggesting that property specific factors are driving the variation.

Table: Average development/acquisition cost per unit by procurement type

HNZ: Average development costs				
NZ\$'000s	1 bedroom	2 bedroom	3 bedroom	4+ bedroom
Auckland				
Turn-key	n/a	452	727	782
Buy-in	513	592	745	791
Redevelopment	325	356	524	589
Total - Auckland	344	400	681	716
Rest of New Zealand				
Turn-key	284	365	560	596
Buy-in	365	347	498	568
Redevelopment	278	340	366	544
Total - Rest of New Zealand	279	350	455	571
New Zealand				
Turn-key	284	390	662	720
Buy-in	476	488	692	755
Redevelopment	288	351	473	582
Total - New Zealand	293	380	622	688

- The sample indicates that HNZ has not acquired any Turn-key 1 bedroom units in Auckland in the period of our sample.
- The comparability of redevelopments relative to the other procurement types is challenging given the treatment of land costs in our dataset. While the data suggests that redevelopment costs per unit are lower, we would caution against drawing broader conclusions from this.
- The dataset shows some impact of construction and property market inflation over the period, with cost increases of approximately 32% in 2016 and 6% in 2017.

Table: Average development/acquisition cost per unit over time

HNZ: Average development cost by year and typology				
NZ\$'000s	1 bedroom	2 bedroom	3 bedroom	4+ bedroom
Auckland				
FY16	n/a	386	558	547
FY17	327	330	645	685
FY18	319	398	678	720
YTD19	357	468	732	793
Total - Auckland	344	400	681	716
Rest of New Zealand				
FY16	261	338	358	426
FY17	234	311	397	488
FY18	295	362	536	576
YTD19	289	423	513	652
Total - Rest of New Zealand	279	350	455	571
New Zealand				
FY16	261	353	445	518
FY17	257	320	558	648
FY18	299	390	659	699
YTD19	309	452	669	754
Total - New Zealand	293	380	622	688

Costs of delivering new Public Housing supply HNZ - Development and acquisition costs (2 of 2)

We have analysed a subset of our development cost data where the land cost can be separated out accurately.

Given limitations in the reliability of the dataset, we consider the results to be indicative only and would caution against drawing broader conclusions.

Key findings

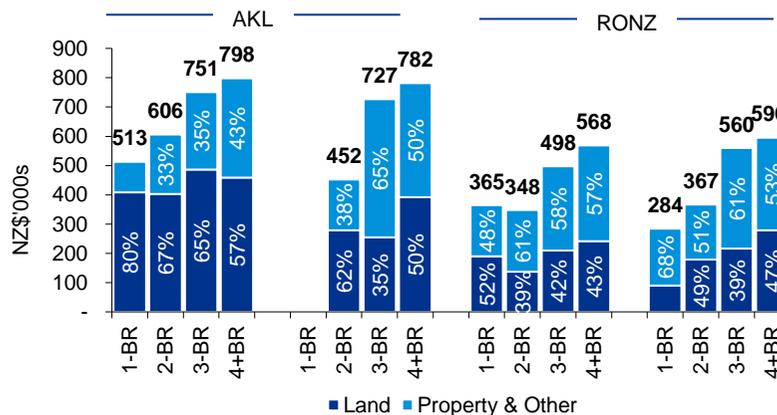
Of the 2,473 properties in our dataset (after removing leases and properties without development cost data), we were provided with separated land and property costs for 1,048 places. We note that:

- The break-down is based on the fixed asset register of HNZ, which we have sought to link to our dataset with the assistance of HNZ Finance team.
- The split between the land value and the capital value of a property may derive from a number of different sources (such as the property developer) as the split is not directly observable in the case of an existing property purchase. The data results should be considered indicative only.

Based on our dataset, we can make the following observations:

- The land proportion of the total acquisition cost is higher in Auckland than the rest of New Zealand, reflecting Auckland's relatively high land costs.

Diagram: Land and building development breakdown



- The cost per sqm costs between Auckland and the rest of New Zealand are relatively similar, indicating that, for similar sized houses, land costs are likely to significantly account for the variation in total cost by region.

Diagram: Average property size by region and procurement type

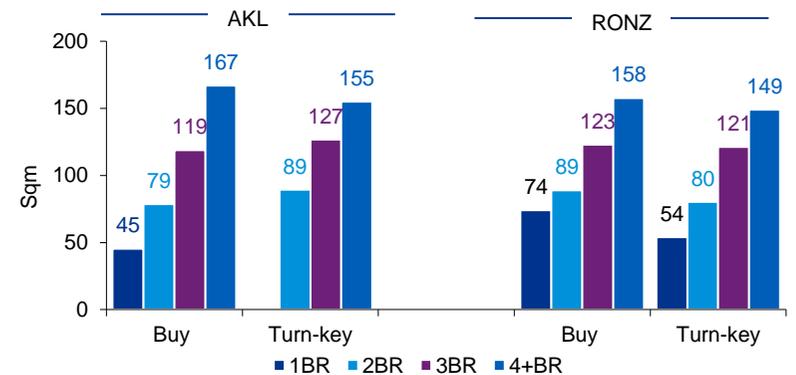
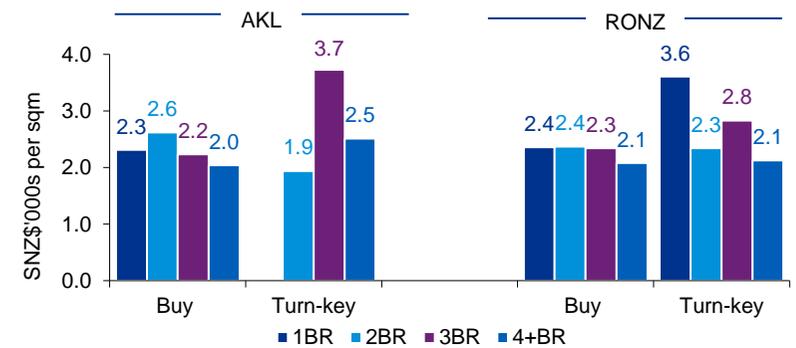


Diagram: Building cost* per sqm by region and procurement type



Costs of delivering new Public Housing supply

Operating cost categories

We sought operational cost data associated with new supply by HNZ and CHPs. Similar to development costs, our data has limitations as indicated on the right.

For CHPs, these are based on forecast costs. For HNZ, these are a combination of actual and forecast costs.

Operating cost categories

The following table sets out the key operational cost categories for the delivery of Public Housing, and an indication of the availability of data within our datasets.

Category	Description	CHP data	HNZ data
Operating costs			
Tenancy and Property Management	Activities can include the allocation of a tenant to a property, tenancy induction and tenancy agreement administration, rent collection, inspections, interactions with tenants to support the sustainability of their tenancy and activities to maintain the condition of properties (such as arranging maintenance).	Available per unit (excl. typology)	Average cost by four regions
Repairs and Maintenance	The cost of responsive repairs (both urgent and non-urgent) and cyclical/planned maintenance.		
Capital replacement	Capital renewals that are required to maintain the market rent value over time. This is typically captured in an annualised amount.		
Rates	Rates payable to the local Council of the property.		
Vacancy	Vacancy refers to the assumed vacancy rate for the property, usually expressed as a % of vacant weeks in a year (sometimes represents a negative revenue line). To improve comparability of results, we have removed vacancy costs from our analysis, except in our commentary on redirects later in this section.	Excluded from analysis	Excluded from analysis
Insurance	The cost of property insurance.		N/A*
Utilities	The cost of utilities (where these are borne by the provider).		
Lease costs			
Lease costs	Lease costs represent the payment to the lessor of the property.		Partial

* HNZ insures on a portfolio basis with a large deductible. A per property insurance would not provide a like for like comparison.

Not available for this review	Partially available for this review	Available for this review
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Costs of delivering new Public Housing supply Tenancy and property management

The forecast cost of tenancy management and property management per unit for CHPs was \$2,236 in our dataset, relative to an average of \$2,494 for HNZ across all its properties in FY18.

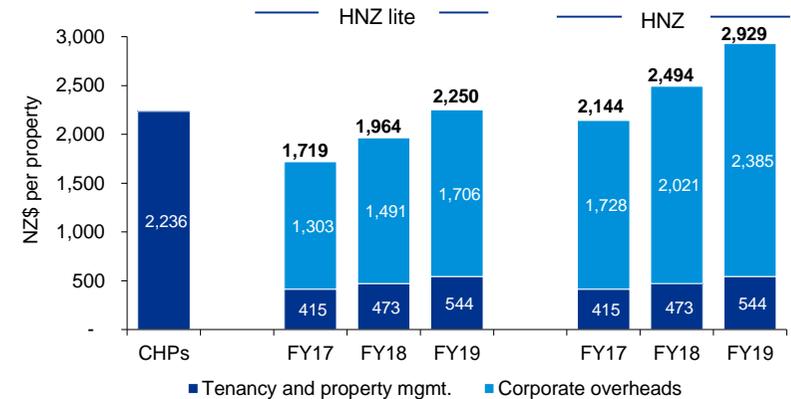
The HNZ figure includes a significant allocation of corporate overhead reflecting its significantly different business model to that of the CHP sector. The comparability is also limited given that the analysis does not control for relative tenancy management service levels.

Key findings

Based on our data, we observe that:

- The average tenancy and property management cost for CHPs per unit was \$2,236. There was significant variation, with the costs ranging from \$676 to \$4,671 per property. This represented between 3.2% to 22.7% of the market rent in the sample properties. We note that the above figures are based on what the CHP allocated to tenancy management, and in some cases may have allocated overhead costs under 'other' costs.
- HNZ provided tenancy and property management costs split by four regions covering all of New Zealand. There was only limited regional variation, with an average cost of \$2,494 per property in FY18. This consisted of direct costs of \$473 and an allocation of corporate overhead of \$2,021.
- We note that HNZ's actual cost is based on management of its entire portfolio, rather than only new supply units. We would therefore expect these to be higher given the likely greater property management overhead required to service an aged portfolio.
- HNZ's tenancy and property management costs have increased from \$2,144 per property in FY17 to \$2,929 in FY19 (based on 9 months data), representing a 37.6% increase over this period. HNZ has sought to intensify its tenancy support services over this time.
- HNZ provided a modified cost per property that it considered would be more reflective of the operating model of a CHP. At a rate of \$1,964 per property in FY18, this 'HNZ lite' estimate removes approximately 27.0% of the overhead component, largely from management of governance groups that a CHP is unlikely to require.
- We note that the above costs are broadly in line with available benchmark costs from Australia and the UK for tenancy and property management. The limitations of benchmarking using existing information are discussed in more detail in section 5.

Graph: Tenancy and property management costs



Note: FY19 HNZ costs are grossed up amounts based on 9-months of data.

Benchmarks: Tenancy and property management cost per unit

Source	Benchmark cost (\$NZD)	Metric (p.a)
2018 Sector scorecard (UK)	\$1536 - \$2345	Management cost per unit
2018 Global accounts (UK)	\$1398 - \$2249	Management cost per unit
	\$1852 - \$3080	Management cost + letting, community services, other activities and support service charges per unit
Pawson (Australia)*		Based on statistics collected on six CHPs using the author's collection framework
- Tenancy management	\$1689	
- Property management	\$740	
- Individual support	\$290	
- Additional services	\$260	
Total	\$2976	
SHRP proposals	\$1,521	Average

*Based on 2013/14 data. Inflated by 1.5% per annum to 2018/19.

Costs of delivering new Public Housing supply

Repairs, maintenance and capital replacement

The forecast average annual cost of repairs and maintenance per new unit for CHPs was \$1,896, based on the CHP benchmark data.

HNZ's repairs and maintenance and capital replacement assumptions are based on the age and typology of the properties, as shown in the tables on the right.

Key findings

CHPs

- The forecast average annual first year repairs and maintenance costs per unit in the CHP data was \$1,896, with a range from \$435 to \$3,645. This represents approximately 0.1% to 1.3% of the total capital value (including land). Our dataset did not allow a typological split of operating costs, and therefore cannot comment on the extent to which typology (or region) explains the variation.
- Only a small number (8 of 36) of the developments in the CHP dataset included a separate capital replacement figure. For those included, the average annual capital replacement assumption was \$1,524 per annum. This effectively reflects the annual amount that the CHP allows for future capital replacement.
- For the eight CHP projects for which we have financial models, we note that annual repairs and maintenance are approximately \$1,600 per property. Six of the financial models assume additional capital replacements of approximately \$2,963 per property. The phasing of capital replacement costs varies between the models, including a indexing annual amount allowed from year 1 and an indexing annual amount from year 15. While not observed in our sample, a modelled replacement profile (i.e. lumpy reflecting large capital spends) is also common in infrastructure projects.

HNZ

- The benchmark tables represent the rates used for HNZ's financial management purposes, allowing variation in the cost assumption based on age and typology of the property.
- The actual combined spend on repairs, maintenance and capital replacements over the last three years have been broadly between \$7,400 - \$7,600 per property.

Table: HNZ repairs and maintenance estimates

HNZ: Repairs and maintenance					
NZ\$ per unit	Number of bedrooms				
	1	2	3	4	5
Age					
0-10	3,302	3,825	4,000	4,218	4,429
11-20	3,876	4,592	4,800	5,080	5,334
21-30	3,985	4,617	4,837	5,089	5,343
31-40	3,774	4,354	4,569	4,802	5,042
41-50	3,884	4,475	4,673	4,911	5,157
51-60	3,778	4,312	4,495	4,698	4,933
61-70	3,908	4,397	4,583	4,773	5,012
71-80	4,388	5,061	5,247	5,481	5,755
80+	4,070	4,685	4,870	5,107	5,362

Table: HNZ capital replacement estimates

HNZ: Capital replacements					
NZ\$ per unit	Number of bedrooms				
	1	2	3	4	5
Age					
0-10	856	938	1,085	1,181	1,240
11-20	1,064	1,151	1,337	1,449	1,521
21-30	1,487	1,668	1,948	2,143	2,250
31-40	1,855	2,118	2,510	2,779	2,918
41-50	2,186	2,515	3,031	3,375	3,543
51-60	2,277	2,702	3,114	3,475	3,649
61-70	2,753	3,300	3,843	4,310	4,526
71-80	2,987	3,638	4,295	4,906	5,151
80+	1,778	2,193	2,357	2,690	2,825

Table: Actual spend for HNZ repairs and capital replacements

	2016/17	2017/18	2018/19
Operating (\$m)	315	319	362
Capital (\$m)	159	155	135
Total (\$m)	474	474	497
Average per property	7,491	7,407	7,616

Costs of delivering new Public Housing supply Repairs, maintenance and capital replacement (cont.) and Other Costs

The available international benchmarks suggest a lower spend per property than the HNZ average, but both benchmarks are based on UK data which has limited comparability with NZ building styles.

In addition to the previous major cost categories, there are a number of other operational costs incurred in the delivery of Public Housing, such as rates and insurance.

Repairs, maintenance and capital replacement (cont.)

Additional comment on benchmarking of repairs and maintenance costs is provided in section 3. In interpreting these benchmarks, however we note that:

- International benchmarks reflect local construction costs and housing building styles (e.g. brick terraced housing in the UK).
- Average cost per unit does not account for differences in age or typology of the portfolio.
- The NZD benchmarks have been converted at the time of this report, and therefore reflect relative currency strength.

Source	Benchmark cost (\$NZD)	Metric (p.a.)
2018 Sector scorecard (UK)	\$1464 – 2118	Maintenance per unit
	\$992 – 1857	Major repairs and capitalised repairs per unit
	\$2457 - \$3976	Total per unit
2018 Global accounts (UK)	\$1493 - \$2211	Maintenance per unit
	\$907 - 1776	Major repairs and capitalised repairs per unit
	\$2400 - \$3987	Total
SHRP	\$6,227	Property management per property. Significant variation was observed

Other costs

Rates

The level of rates charged to a property are a function of the value of the property (as assessed by the local Council) and the Council's rates policy. We would not expect to see any provider variation in the level of rates.

Water rates and utilities

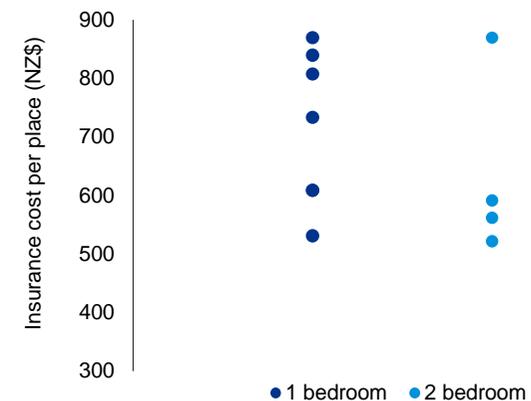
In some instances, there is a utilities cost borne by the provider where these are not separately paid by the tenant. From our CHP sample, 13 developments included a cost allowance for utilities, representing approximately 5.8% of total operational costs. HNZ covers the cost of water rates where these are billed by the Council.

Vacancy provision

We note that both CHP and HNZ costs generally include a provision for vacancy costs – periods where the property is not receiving a market rent. This is generally in the order of 3% of market rent when included in the CHP dataset. HNZ typically uses a 0.5% vacancy assumption for investment purposes.

Insurance

The CHP dataset includes an assumed insurance cost, which ranged from \$522 to \$870 per annum. HNZ insures its properties on a portfolio basis with a large deductible.



Costs of delivering new Public Housing supply

Summary operational costs per unit

This page provides a summary of the total operational costs of the new supply properties in our datasets for CHPs and HNZ.

Please note the caveats on previous pages regarding the allocation of costs to particular units and the current limitations in comparing directly costs between HNZ and CHPs (e.g. different business models, tenant cohorts).

CHPs operational cost summary

CHPs: Operating costs per per place for the build and turn-key procurement types								
		Year one total operating cost (NZ\$ per place)						
Procurement type	No. of places	Tenancy management	R&M	Rates	Insurance	Other operating costs	Sample size	Cost per place (\$)
Turn-key	127	2,202	1,728	1,447	577	203	11	6,157
Build	397	2,433	2,136	1,666	687	890	12	7,812
CHPs	524	2,377	2,037	1,613	660	723	23	7,411

* Examples of other operating costs include utility expenses, although there is variability between CHPs.

HNZ operational cost summary

HNZC: Operating costs per place by region for the build, buy and other procurement types							
		Average operating cost (NZ\$ per place)					
Region	Number of places	Tenancy management	R&M - Operating	R&M - Capex	Rates	Corporate overheads	Total opex per place (\$)
Auckland	1,679	473	4,198	1,302	1,379	2,385	9,738
Canterbury	544	477	3,713	964	1,734	2,385	9,273
Waikato	223	477	3,993	1,064	1,638	2,385	9,557
Hawke's Bay	91	529	4,109	1,626	174	2,385	8,824
Wellington	72	541	3,645	1,374	652	2,385	8,597
Manawatu-Wanganui	37	531	4,240	1,549	1,902	2,385	10,607
Bay of Plenty	25	546	4,008	1,121	2,040	2,385	10,100
Marlborough	21	546	4,013	1,136	2,096	2,385	10,176
Other regions	76	515	3,965	1,175	1,563	2,385	9,604
Total - New Zealand	2,768	481	4,060	1,226	1,435	2,385	9,587

* The relatively low rates in Hawke's Bay and Wellington are due to data limitations in our sample.

Costs of delivering new Public Housing supply

Cost of capital and CHP financing arrangements (1)

For Public Housing investment decision making purposes, HNZ's applies a cost of capital assumption of 5.89%, based on analysis undertaken by Deloitte.

Introduction

The construction or purchase of properties requires an upfront capital outlay, typically either through milestone payments during works or upon completion. This capital cost can be met either from the provider's balance sheet or via new debt and/or equity financing. The average cost of its capital sources is captured by the Weighted Average Cost of Capital (WACC). It represents the rate of return required from an organisation's investments in order to maintain the organisation's value.

HNZ's cost of capital

For the purposes of investment decision making, HNZ's WACC for Public Housing developments is 5.89%. This is based on a cost of capital review undertaken by Deloitte in April 2017. This compares with a WACC of 8.68% (mid-point) for mixed residential developments, given the greater commercial risk associated with such projects.

We have not reviewed the inputs into Deloitte's calculations as it is not within the scope of this work, however the methodology appears typical for a cost of capital review.

WACC

The calculation of HNZ's WACC is based on an average of values between 2003 to 2015. The standard formula for WACC is:

$$WACC = (\% \text{ equity capital} \times \text{cost of equity}) +$$

$(\% \text{ debt capital} \times \text{cost of debt})(1 - \text{taxation rate})$
Cost of debt: The cost of debt has been derived with reference to the 10-year government bond yield over the period (3.4% average)

Cost of equity: The cost of equity is derived through a calculation of expected returns from assets given the risk of those assets and the risk-free return rate.

Leverage: The leverage assumption is 88% equity financed and 12% debt financed, based on an earlier cost of capital review undertaken by Deloitte.

We note that HNZ is not currently expected to pay a dividend to the Crown, with surplus cash from operations set out in its LTIP being used to support new supply and redevelopment.

HNZ's cost of capital is a key input into its investment decision making and the calculating of OS. This is outlined in further detail in section 6.

Costs of delivering new Public Housing supply

Cost of capital and CHP financing arrangements (2)

There is a no single CHP cost of capital given the diversity of organisations within the sector.

CHP cost of capital and financing arrangements

We have summarised available evidence on CHP cost of capital and financing arrangements below.

CHP gateway 2 models

Based on the eight gateway models, the following table provides a high-level summary of key financing arrangements and terms. In summary, we note that the cost of debt is broadly within 5% to 7%. There is a reasonable range of leverage levels, although typically they are between 50 – 75%.

Overview of CHP financing arrangements				
CHP project	1	2	3	4
Capital (NZ\$'000s)	14,870	8,501	4,130	14,284
Cost of debt (year 1-3)	5.5%	5.5%	6.5%	6.0%
Cost of debt (year 4+)	6.5%	6.5%	6.5%	7.0%
Leverage	75.0%	75.0%	67.0%	50.0%
Upfront funding	none	none	10.0%	none
Loan (NZ\$'000s)	11,152	6,376	2,767	7,142
CHP project	5	6	7	8
Capital (NZ\$'000s)	12,986	9,660	595	2,384
Cost of debt (year 1-3)	5.5%	6.1%	6.5%	4.3%
Cost of debt (year 4+)	6.5%	7.0%	6.5%	4.3%
Leverage	0.0%	50.0%	76.0%	50.0%
Upfront funding	none	50.0%	none	none
Loan (NZ\$'000s)	-	4,830	452	1,192

Note: Capital cost include GST. Leverage is defined as Debt/(Debt + Equity + Upfront Funding). Where leverage is 0%, no bank finance is included in the proposal.

Social housing transfers

A summary of key financing terms from proposals submitted during the SHRP transfers (Tauranga, and the proposed Invercargill and Christchurch transactions) is below. The required equity return predominately represents that of investors seeking to invest in an existing aged portfolio within the commercial parameters of the SHRP.

	Range	Average
Gearing	73% - 87%	82%
Capital growth assumption	0% - 4%	2.4%
Equity IRR	8.5% - 16%	11.2%
Equity IRR (excl. residual value)	5.8% - 13.3%	9.6%

Further, we are familiar with a Council housing transfer where the equity investor required return was approximately 8% p.a., including the residual value at the end of the contract term.

Comment

- Where a development is funded from a CHP's own resources (i.e. philanthropic funds), it could be argued there is no associated cost of equity. The return is primarily social, rather than monetary, and the funders of the CHP have no expectation of a return. Alternatively, a CHPs may consider its WACC to simply be its cost of debt. In both cases, this would likely underestimate the CHP's true cost of capital and may potentially lead to the overuse of debt. If policy settings do not account for a CHP's cost of equity, it is unlikely that the sector will attract significant further investment from external capital sources.
- Given the above assumptions, i.e. cost of debt of 5-6%, cost of equity of 8 – 11%, and leverage of 70%, this would equate to a WACC of broadly 6 - 8%.

Costs of delivering new Public Housing supply CHP redirect properties

Redirects are a key component of recent CHP new supply. These do not qualify for OS, with the only cost to the Crown being IRRS.

In many cases, HUD pays a management overhead (broadly 8-20%) for some redirect properties via the IRRS.

Introduction

Redirect is a catch-all term for Public Housing supply that hasn't come through HUD's new supply programme. These are predominately provided by CHPs through lease arrangements with private landlords, but may also include properties made available from existing CHP stock (e.g. donated, purchased, building no longer required for wider mission of the CHP, properties funded through the SHU). For leased properties, a CHP will generally add an overhead component to the lease cost it pays for a property to cover its own management costs. Under current practice, this can sometimes result in a total rent in excess of the current rent maxima.

Redirects are responsible for the bulk of additional new IRRS supply that CHPs have brought on in the last 3 years.

Data limitations

- There is no requirement for a CHP to submit to the HUD the lease cost payable to the private landlord. Accordingly, there is a lack of data on the level of overhead mark-up applied to redirect properties, however HUD estimates this to be in the order of 8 – 20% of the market rent.
- The contractual obligations of the CHP under its own lease arrangements will vary – there is no standard form agreement used by CHPs for redirect properties. However, it is understood that the obligations of the CHP are broadly similar to those of a regular private tenancy arrangement, although with an additional insurance charge given the hand-back requirement at the end of the tenancy.

Redirect market rent and overhead payment

- We understand that the overhead payment is charged to HUD through a number of different mechanisms, including a flat amount per property, a percentage of market rent or a per property by property fee.
- Based on indicative analysis, leased properties of the same TLA and typology generally have higher determined market rent than CHP owned properties (indicatively 4 – 22% in Auckland). However, the data does not allow the driver of this to be determined.

Benchmarking the redirect overhead component

We have not completed a comprehensive benchmarking exercise, however we have done an indicative sense check of the 8 – 20% overhead that HUD believes it is currently paying.

For the purposes of this exercise, we have assumed that the CHP would remain responsible for:

- tenancy and property management.
- additional insurance (although we do not have an available estimate of these costs) and vacancy risk.

All other costs are assumed to be covered by the private landlord. We note that private tenancy management is typically in the order of 8-12%, suggesting a 8-20% overhead is broadly similar for the private sector (although the level of service would typically be lower than that required to be provided by a CHP). Our indicative benchmark below also indicates that the current management overhead is broadly within an expected range.

Similar to the case of a regular property manager, it would be expected that a landlord should receive a lower payment (given the CHP manages the property) than if the landlord managed the property themselves.

	Estimate	Comment
Average market rent	\$15,000 - \$27,000	Based on \$300 to \$550 per week, with 5% vacancy
CHP costs	Tenancy and property management: \$2,236	We do not have an estimate of insurance costs, although would not expect these to be material to this exercise.
CHP costs as a proportion of market rent	8 – 15%	Indicative only, subject to specific lease arrangements.

Costs of delivering new Public Housing supply

Economics of new supply projects and whole of life costs (1 of 4)

This section provides observations on the economics of new supply projects. In particular, it uses an illustrative example to show the impact of a development on key financial investment metrics.

Introduction

Previous work by government agencies has led to initiatives to support the development of new Public Housing supply. This has been on the basis that market rent alone is not sufficient to support commercially viable developments given land and development costs. In essence, market rent reflects elevated market expectations of capital gains that a Public Housing provider would not realise, but that a private developer would. This section describes different perspectives on the economic viability of new supply.

Perspectives on project economics

There are a number of standard investment metrics to consider the viability of an investment.

- **Project NPV:** A measure of the total project cash-flows discounted by the WACC of the provider over the life of the asset. A NPV>0 would indicate an economically viable project, although assumes that the provider can access capital as required.
- **Equity IRR:** A measure of the return received by the equity investor (i.e. operational net cash-flows less debt servicing). This should meet or exceed the required rate of return of the investor.
- **ICR (Interest Coverage Ratio):** A measure of an entity's ability to cover its interest costs from its operating surplus. Typically, banks would look for a minimum of around 1.5 as part of its due diligence.
- **Incremental return on investment (IROI):** The primary measure used by HNZ for new supply investment decisions. This is outlined in more detail in section 6.

Residual value

A residual value for the property at the end of the period accounts for the value remaining in the property at that time. This can either be the projected capital value of the property (based on an assumed capital growth rate) or the present value of renting the property indefinitely.

Illustrative whole of life costs

We have undertaken simple whole of life analysis to demonstrate the economics of new supply for an illustrative development.

Key assumptions

The illustrative development is a two-bedroom unit development in Auckland, with assumptions broadly derived from the earlier cost analysis. The residual value is based on the property hypothetically being sold at the end of the period.

Item	Assumption
Market rent (weekly)	\$550
Vacancy rate	0.5%
Development cost	\$550,000
Rates p.a.	\$1300
Insurance p.a.	\$800
R & M p.a.	\$2000
Tenancy and property management p.a.	\$2300
Capital replacement p.a.	\$900
Rental and cost growth p.a.	2%
Capital growth p.a.	2%
Cost of debt	6%
Cost of equity	9%
Leverage	70%
Crown discount rate	6% (nominal)

Costs of delivering new Public Housing supply

Economics of new supply projects and whole of life costs (2 of 4)

The metrics on this page are based on an indicative whole of life cost for a two-bedroom development in Auckland, without any additional subsidy.

Key project metrics

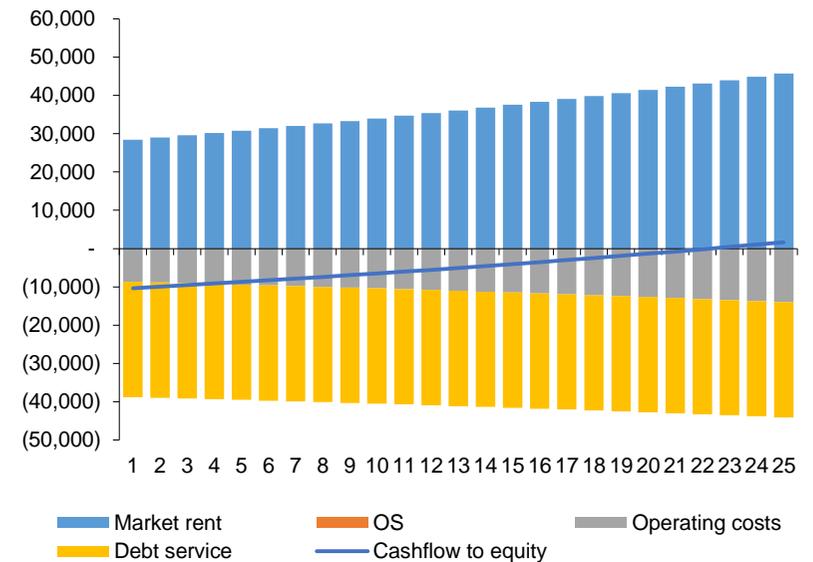
The following table provides a summary of key project metrics given the earlier assumptions. The discount rate for the project is 6.90% given the leverage and return requirements set out in the previous page.

Project metric	Value
Operating costs as % of income (yr 1)	31%
Net operating cash-flow (yr 1)	19,757
Gross rental yield (yr 1)	5.2%
Cash-flow to equity (yr 1)	(10,360)
Total borrowing required	385,000
Project IRR	5.59%
Project NPV	(94,830)
Equity IRR	5.30%

Comment

- The sample project is intended to illustrate the economics of a development given a certain set of assumptions. While the project does generate a significant operating surplus in each year, this is not sufficient to meet debt servicing costs. This is represented by a negative cash-flow to equity over the period.
- The ICR is below 1.5 for the first decade of the project which is unlikely to be considered sufficient by a bank. The cash-flow position does improve over the period as debt servicing remains constant in nominal dollars, while net operational cash-flow improves through inflation.

Diagram: Project cash-flows



- The project does not have a positive NPV (i.e. the returns do not meet the project's WACC). Even if the provider could meet the cash-flow shortfall from other sources, the project does not meet the required rate of return and therefore, purely on a financial basis, the project would not be economically viable from the perspective of the provider.

Costs of delivering new Public Housing supply

Economics of new supply projects and whole of life costs (3 of 4)

We adjusted our scenario to include a 50% upfront payment to the provider.

This changes the economics of the project by lowering the required borrowing and debt servicing costs.

Impact of 50% upfront payment

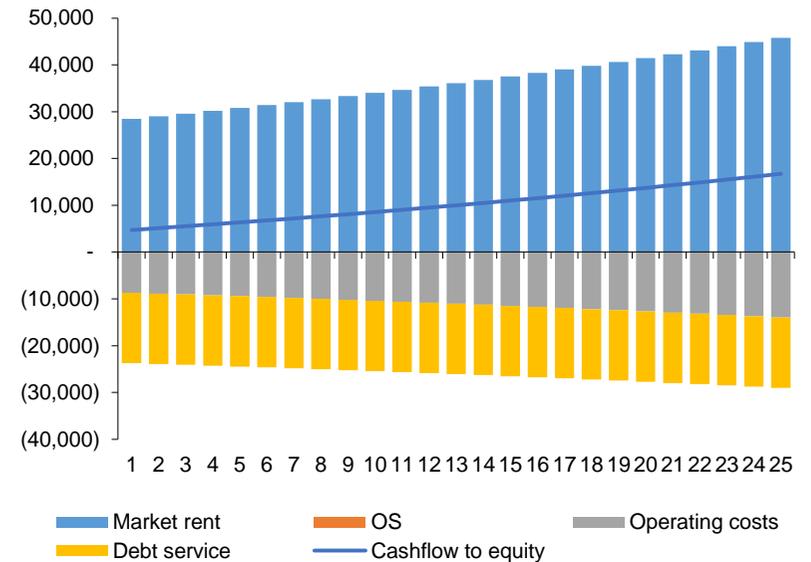
For the purposes of this example, we have assumed that the government provides a 50% upfront payment for the development. Assuming gearing remains the same as in the previous scenario, this reduces the level of borrowing from 70% of the development costs to 35%, with the remaining 15% being equity from the provider.

Project metric	Value
Operating costs as % of income (yr 1)	31%
Net operating cash-flow (yr 1)	19,757
Gross rental yield (yr 1)	5.2%
Cash-flow to equity (yr 1)	4,698
Total borrowing required	192,500
Project IRR	5.59%
Equity IRR	14.22%

Comment

- The inclusion of an upfront payment changes the project economics from the provider's perspective. While revenue for the project remains the same as the prior example, the lower borrowing level and therefore lower debt servicing means that the project has consistent positive cash-flows over the 25 year term.
- The project maintains an ICR of 1.7 from year 1, growing over time. This would typically meet a bank's due diligence requirements.

Diagram: Project cash-flows



- Under the assumptions in our example, a 50% upfront payment results in the project and equity IRRs exceeding the required rates of return.

Costs of delivering new Public Housing supply

Economics of new supply projects and whole of life costs (4 of 4)

We also adjusted the base scenario to include a 50% operating subsidy in addition to market rent.

While private borrowing is the same as the base scenario, it significantly increases revenue for the provider.

Impact of 50% operating subsidy

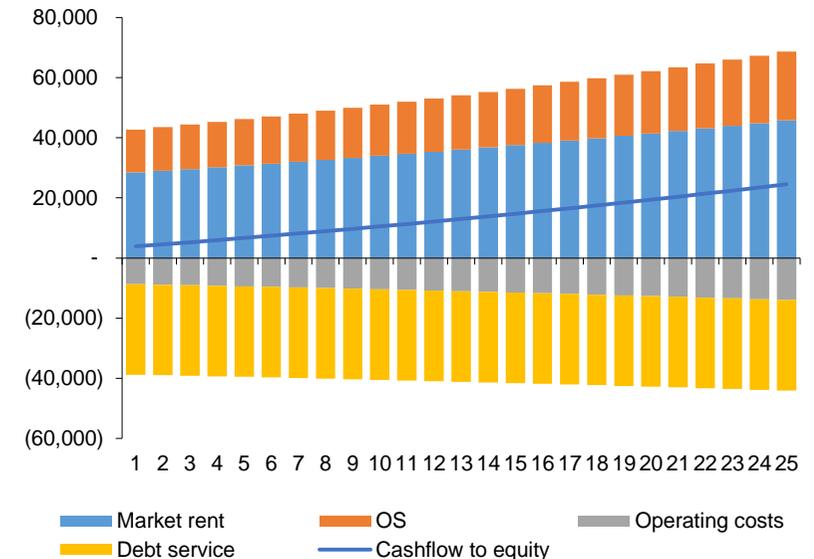
For the purposes of this example, we have included an operating subsidy of 50% market rent. This is the typical level of OS that has been approved for CHP developments in Auckland under Build and Turn-key procurement types.

Project metric	Value
Operating costs as % of income (yr 1)	31% (20% incl. OS)
Net operating cash-flow (yr 1)	33,986
Gross rental yield (yr 1)	7.8%
Cash-flow to equity (yr 1)	3,868
Total borrowing required	385,000
Project IRR	8.18%
Equity IRR	10.19%

Comment on economics including 50% UF

- The level of borrowing and debt service costs remain the same under the base scenario, but the subsidy provides significantly greater cash-flow to the provider to cover debt servicing costs.
- Under the above assumptions, the subsidy enables the project to meet its key investment metrics that would enable the project to be viable. The return to equity exceeds the target return.

Diagram: Project cash-flows



Operating subsidy and upfront payment - Cost of the Crown

The two alternative scenarios presented are not calculated on the basis of providing an equal level of subsidy, but do reflect the common values for recent developments. Given the inputs in our example, the cost to government of the upfront payment is greater than the operating subsidy. This is not a general finding on the relative cost of these two mechanisms. If the CHP development cost for the property was \$440,000 (rather than \$550,000), the cost to government between the two approaches would be the same, all else being equal.

Project metric	Lifetime cost to Crown
Upfront (50% of development costs)	\$275,000
Operating subsidy (50% of market rent)	\$219,738

3

Public Housing government
expenditure and value for money

Public Housing government expenditure and value for money

Introduction and approach

This section sets out our analysis of available evidence on government expenditure and value for money in Public Housing.

The existing data on the performance of the CHP sector is relatively limited, although we have attempted to supplement this through a CHP survey conducted in June 2019.

Introduction

This section sets out our analysis of recent government expenditure on Public Housing. While the previous section primarily focused on the costs faced by providers, this section focuses on the costs incurred by government through various funding streams. In addition, it seeks to set out the available evidence on the value for money the government has received from this expenditure.

Approach

Government expenditure overview

The government expenditure analysis focuses on:

- Setting out the key funding streams for Public Housing, and a high-level commentary on their movements.
- A brief summary of two historic programmes to support the delivery of new supply – the Housing Innovation Fund (HIF) and the SHU Fund.
- A discussion on the expenditure and outcomes of recent incentives for new supply – OS and UF.

Value for money analysis overview

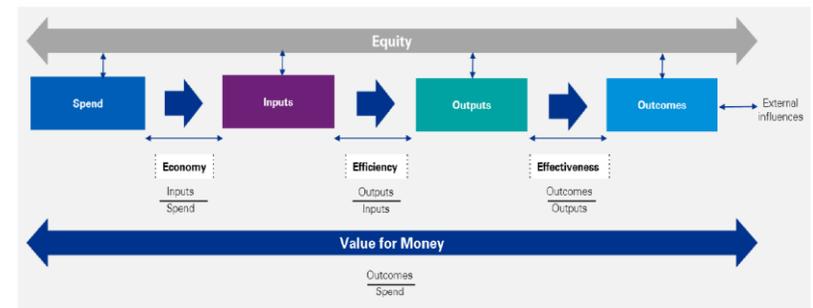
The value for money analysis focuses on:

- The development of a value framework for considering value for money of Public Housing.
- Development of a set of metrics to consider value for money across Public Housing.
- Collection of data on the above metrics, where available.
- Drawing conclusions based on that data.

Value for money framework

Our value for money framework* is based on a typical '3Es' approach to measuring value for money. In particular, it considers metrics in the following categories:

- **Economy:** level of input costs
- **Efficiency:** spend to outputs
- **Effectiveness:** achieving desired outcomes



Where data allows, the data collected against the metrics in the above categories are compared against a benchmark.

As described in more detail further, current data to assess value, particularly in the CHP sector, is relatively limited. To supplement existing data, we conducted a survey of the CHP sector to collect additional information, which we describe in this section of the report and section 6

* Note that FPDG apply a separate value for money framework for evaluating new supply CHP delivery proposals. This provides a weighted score across ability to deliver, fit for purpose, financial viability and price.

Public Housing government expenditure and value for money

Government expenditure summary (1 of 8)

The adjacent table sets out the movement in government expenditure over the last three years.

Total IRRS expenditure has risen from \$724m in 2015 to \$934m in 2018, a 28% increase. Over the same period, the number of Public Housing places grew by 6.1%.

Historic government expenditure summary

Table: Government expenditure on public housing

MSD: Total appropriations (year ending)							
NZ\$'000s	Dec-15	Jun-16	Dec-16	Jun-17	Dec-17	Jun-18	Dec-18
Funding							
IRRS	724,400	755,396	784,827	814,882	850,778	888,191	930,616
Housing First	-	-	-	31	420	1,209	2,917
Operating supplement	-	4	73	387	702	800	867
Total operating funding	724,400	755,400	784,900	815,300	851,900	890,200	934,400
Upfront funding				42,000			
Number of tenancies							
CHPs	369	3,064	3,270	4,649	4,979	5,339	5,935
HNZ	61,102	57,887	58,635	58,277	58,503	58,973	59,290
Total	61,471	60,951	61,905	62,926	63,482	64,312	65,225
<i>IRRS per tenancy - CHPs</i>	12.45	15.66	15.97	14.84	14.92	14.92	15.17
<i>IRRS per tenancy - HNZ</i>	12.22	12.54	12.88	13.34	13.82	14.40	14.63
<i>OS places</i>		11	75	138	143	163	176

OS is not recorded separately in the IRRS appropriation, and as such, expenditure and OS places is an estimate from MSD.

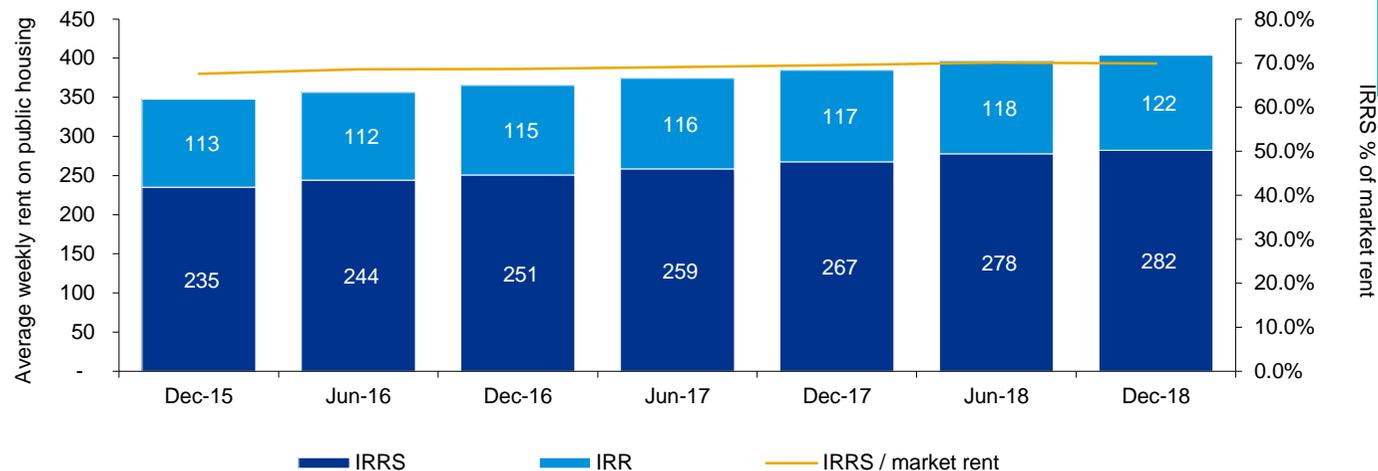
Approximately \$42m of UF drawn down to date.

While rent setting between HNZ and CHPs differ (see section 6), differences in average IRRS per place will be significantly impacted by the size, location and condition of properties, and is not a reflection of relative efficiency of different providers.

Tamaki transfer

Tauranga transfer

Graph: Average weekly rent split



Public Housing government expenditure and value for money

Government expenditure summary (2 of 8)

Based on data provided by MSD, we have sought to disaggregate the movement in revenue between price and volume.

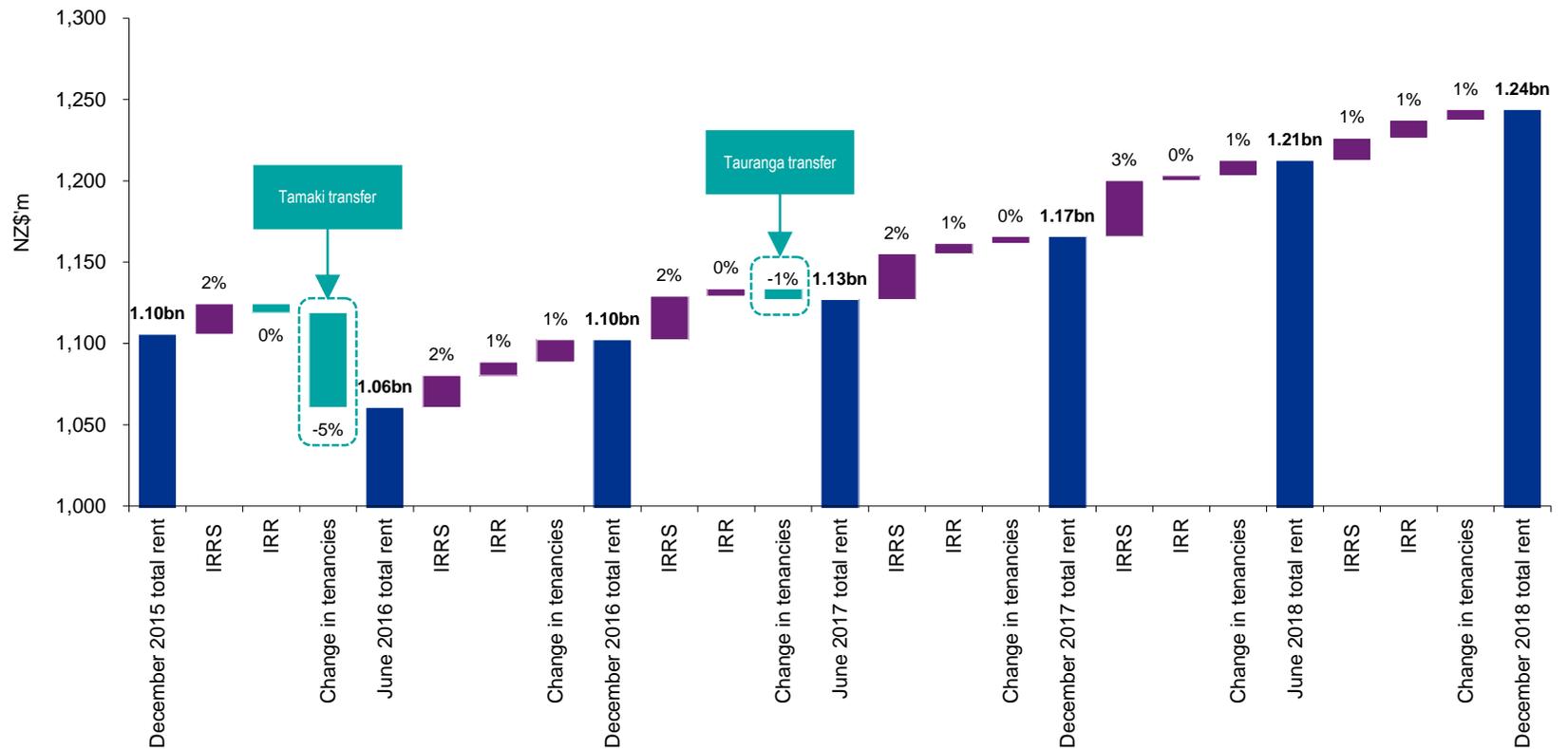
This is presented as a 'bridge' showing the relative contribution to movements in the total revenue between changes in Public Housing units, IRR and IRRS.

Composition of total revenue movement for HNZ

HNZ Public Housing revenue increased from \$1.10bn to \$1.24bn per annum between December 2015 and December 2018. The growth in revenue appears to have been largely market rent driven, with the increase in rent more than offsetting a reduction in the number of tenancies of approximately 1,812. We explore the extent to which the change in total market rent revenue is driven by rental inflation or changes in typology on pages 39-40.

Note that the figures below will not reconcile to actual IRRS expenditure as this analysis is based on 6-monthly data and does not reflect movements in the portfolio between these bi-annual periods.

Diagram: HNZ market rent movement (2015-2018)



Public Housing government expenditure and value for money

Government expenditure summary (3 of 8)

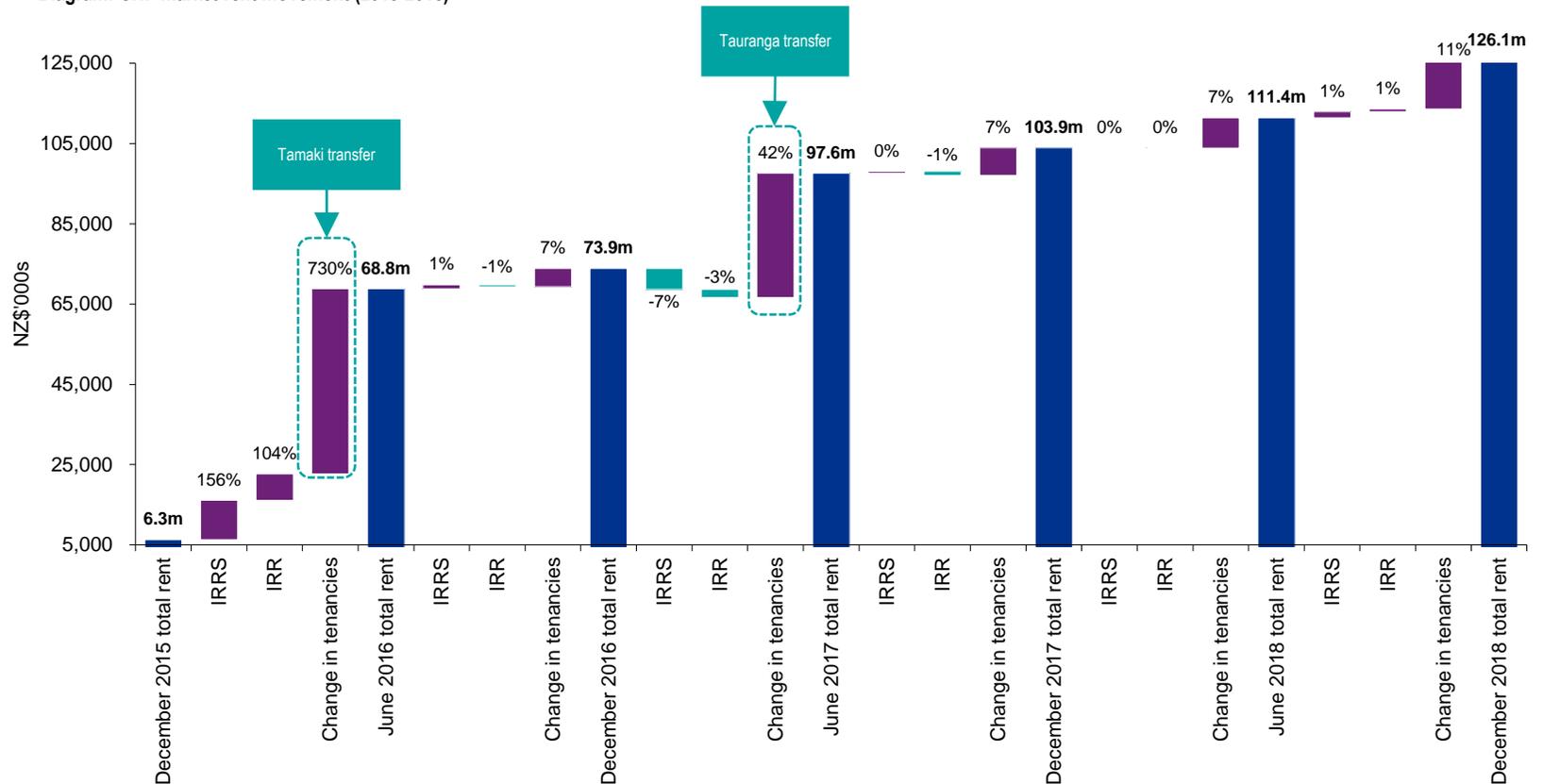
The total revenue of the CHP sector has increased largely through significant increases in the supply of units through the Tamaki and Tauranga transfers.

Composition of total revenue movement for CHPs

The growth in total revenue in the CHP sector has been predominately driven by an increase in the number of Public Housing units, with increased tenancies driving \$108.4m of the \$119.8m increase in revenue. We explore the extent to which the change in total market rent revenue is driven by rental inflation or changes in typology on pages 39-40.

Note that the figures below will not reconcile to actual IRRS expenditure as this is based on analysis of 6-monthly data and does not reflect movements in the portfolio between these bi-annual periods.

Diagram: CHP market rent movement (2015-2018)



Public Housing government expenditure and value for money

Government expenditure summary (4 of 8)

The analysis of typology over time indicates that the results on the previous pages are partially driven by a shift in CHP typology towards smaller properties between 2016 to 2018, rather than rent setting. As would be expected, HNZ's portfolio composition is more stable over the period than for CHPs.

Typology composition over time

We have considered the change in typology composition within the CHP and HNZ portfolios over the last three years. On the following page, we compare movement in rent between HNZ, CHPs and market information by typology and region.

CHP: Typology over time								
Typology	31Dec2015		31Dec2016		31Dec2017		31Dec2018	
	%	#	%	#	%	#	%	#
1	40.92%	151	17.46%	571	22.53%	1122	27.70%	1644
2	40.92%	151	35.26%	1153	34.71%	1728	32.55%	1932
3	11.65%	43	37.46%	1225	34.00%	1693	31.14%	1848
4	6.23%	23	7.71%	252	6.89%	343	6.62%	393
5+	0.27%	1	2.11%	69	1.87%	93	1.99%	118
Total	100.00%	369	100.00%	3270	100.00%	4979	100.00%	5935

Subsequent to the Tamaki transfer, there has been a shift in CHP typology over time to smaller properties (which will lower total rent revenue) and partially explains the result on the previous slide.

Tamaki transfer

HNZ: Typology over time								
Typology	31Dec2015		31Dec2016		31Dec2017		31Dec2018	
	%	#	%	#	%	#	%	#
1	9.13%	5,577	9.10%	5,337	9.10%	5,325	9.26%	5,488
2	37.98%	23,206	38.61%	22,637	38.50%	22,522	38.58%	22,873
3	41.54%	25,379	40.49%	23,744	40.48%	23,683	40.03%	23,733
4	9.12%	5,571	9.40%	5,514	9.53%	5,574	9.73%	5,768
5+	2.24%	1,369	2.39%	1,403	2.39%	1,399	2.41%	1,428
Total	100.00%	61,102	100.00%	58,635	100.00%	58,503	100.00%	59,290

The typology composition of the HNZ portfolio has been broadly consistent over the period.

Public Housing government expenditure and value for money

Government expenditure summary (5 of 8)

Rental movement by typology and region

The table below compares rental movements between CHPs and HNZ by region and typology. The results are intended to be highly indicative only based on data provided by MSD and MBIE rental data. Some regions are excluded from the MBIE data given they are different regional grouping than provided in the MSD data.

	CHP sector weekly rent average					HNZ weekly rent average			MBIE lower quartile rent			MBIE mean rent		
	Jun-16 units	Dec-18 units	Jun-16	Dec-18	Rent CAGR %	Jun-16	Dec-18	Rent CAGR %	Jun-16	Dec-18	Rent CAGR %	Jun-16	Dec-18	Rent CAGR %
1 bedroom														
Auckland	346	821	288	339	6.7%	311	358	5.7%	328	347	2.2%	383	405	2.2%
Bay of Plenty	12	87	223	239	2.9%	210	244	6.2%	215	284	11.8%	254	320	9.6%
Canterbury	57	551	273	231	-6.3%	211	240	5.3%	189	191	0.4%	238	255	2.7%
Central	-	-			-	156	200	10.4%						
East Coast	5	33	190	251	11.9%	176	240	13.1%						
Northland	-	-			-	163	213	11.2%	181	210	6.0%	200	223	4.4%
Southern	-	8		238	-	170	184	3.2%						
Taranaki	6	12	181	224	8.9%	198	234	6.9%	176	193	3.8%	199	231	6.0%
Unknown/Other	2	1	238	174	-11.7%	213	222	1.7%						
Waikato	40	73	184	227	8.9%	205	236	5.7%	185	231	9.3%	216	263	8.2%
Wellington	11	53	199	270	13.0%	223	296	12.0%	259	315	8.2%	309	365	7.0%
West Coast Tasman	-	5		243	-	185	218	6.9%						
2 bedrooms														
Auckland	957	1,171	417	455	3.6%	392	445	5.2%	412	447	3.2%	458	498	3.4%
Bay of Plenty	6	495	318	312	-0.8%	267	307	5.8%	268	338	9.7%	304	379	9.2%
Canterbury	62	135	362	355	-0.8%	327	328	0.2%	298	304	0.9%	336	340	0.5%
Central	-	3		240	-	195	253	10.9%						
East Coast	16	32	239	308	10.7%	228	290	10.1%						
Northland	-	-			-	231	279	7.8%	237	298	9.6%	260	331	10.1%
Southern	2	5	318	480	18.0%	233	251	3.1%						
Taranaki	1	1	220	250	5.2%	246	278	5.1%	249	271	3.4%	276	302	3.6%
Unknown/Other	4	2	386	406	2.0%	324	266	-7.6%						
Waikato	19	28	328	338	1.3%	282	335	7.1%	253		7.8%	280	338	7.8%
Wellington	19	54	328	341	1.6%	299	365	8.3%	333	404	8.0%	376	456	8.0%
West Coast Tasman	3	6	347	360	1.5%	270	294	3.5%						

Although some CHP/HNZ rent increases appear higher than market, absolute rent levels are generally lower than the mean rent levels

Movements in average CHP rentals are influenced by significant percentage increases in the number of properties over the period in particular regions

Public Housing government expenditure and value for money

Government expenditure summary (6 of 8)

Assuming all current pipeline projects are completed, UF will have supported the development of 582 places, at a cost to the Crown of \$110m.

The data suggests a reasonably high-level of variation in UF per new unit of new supply, driven by the variation in development costs across the dataset.

UF

UF provides upfront funding to CHPs to support the development of new build and turn-key supply. UF is generally no longer available for new developments due to funding constraints.

Based on our dataset, we can make the following observations:

- UF has been approved for the delivery of 582 places across 27 projects, of which 547 are located in Auckland. As at the end of June, 137 places have been delivered, with the remaining 445 in the pipeline. Of the 27 developments, 21 were Build projects, with the remaining six being Turn-key purchases
- The total level of approved upfront funding in the current pipeline is \$110m, of which approximately \$42m has been drawn down to date. The majority of places (327) are due to be delivered by the end of calendar year 2019, with the remaining properties due for completion by 2021. The vast majority of new units are 1 and 2 bedroom.
- Of the 27 developments in the UF pipeline, four developments were a combination of both UF and OS (with the OS level ranging from 14% to 33%).
- After excluding an outlier and developments that received a combination of UF and OS, the average UF per unit across all properties in the sample is \$196k, ranging from \$95k to \$290k. The gross rental yield (annual rent as a proportion of development cost) averaged 6.3%.
- We understand that recent UF funding (and all the UF developments in our dataset) has been set at 50% of the development/market value, indicating a total development value of approximately \$220m.

Note: The predominance of UF enabled properties in Auckland is driven by UF only being available in Auckland prior to Budget 2018.

Diagram: Average UF per unit

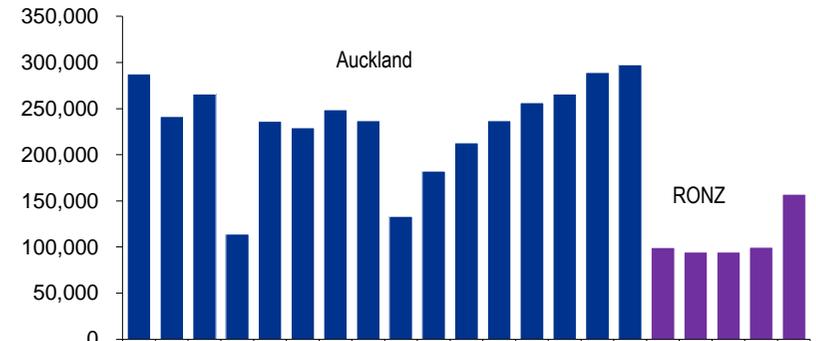
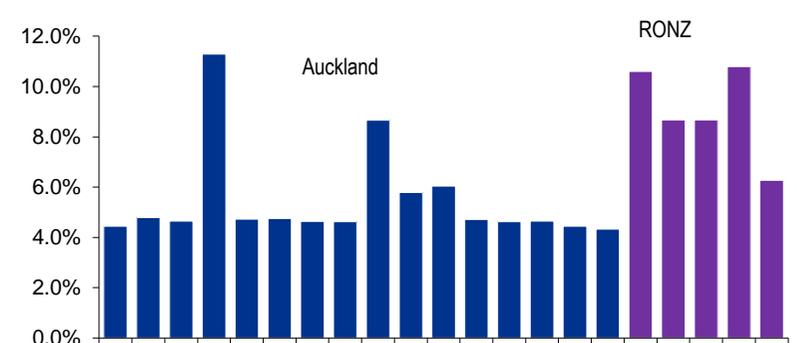


Diagram: Gross rental yield



Cancelled projects

In addition to the above, our dataset includes 22 developments covering 569 units that HUD has marked as not proceeding (or may not proceed) due to a lack of UF.

HUD notes that it has communicated the policy change to CHPs over the last 12 months. Therefore it is difficult to determine the number of projects (i.e. projects that have been put on hold prior to engagement with HUD) that could have proceeded if UF had been available.

Public Housing government expenditure and value for money

Government expenditure summary (7 of 8)

The level of OS agreed to date has been largely consistent at around 50% of market rent, although lease developments have been noticeably lower.

Market rent assumptions have generally been, for Auckland properties, at the current maxima.

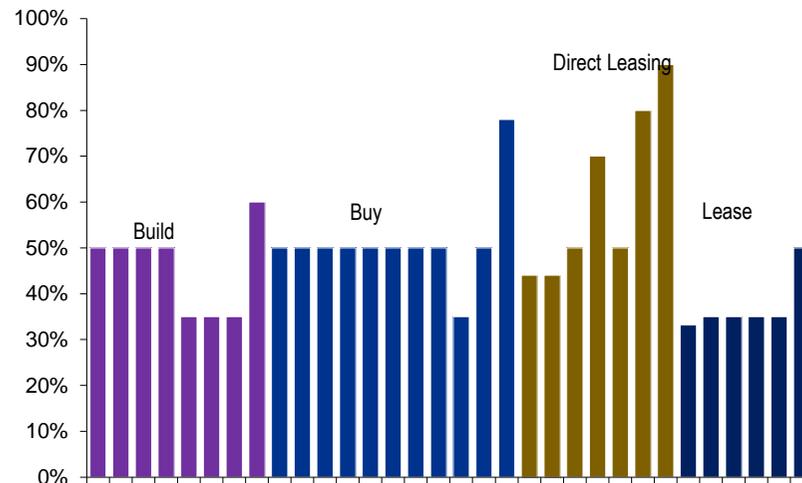
OS

OS has been agreed for approximately 39 of the 69 CHP developments in the agreed new supply pipeline, supporting the development of over 730 units. We understand that HUD is still finalising arrangements with HNZ regarding OS for its units. Under current arrangements, HUD enters into a 25 year capacity contract which includes the payment of the agreed OS % on top of market rent over the contract term.

For the purposes of our analysis below, we have used the slightly smaller CHP 'benchmarking' dataset. This data includes 32 developments that have received OS only (as opposed to a combination of both OS and UF).

Spread of OS% across developments (procurement type)

A simple average across developments indicates that the average OS% was 49%. There is broad consistency across Build and Turn-Key procurement types, although the OS% for lease developments appears consistently lower than others.



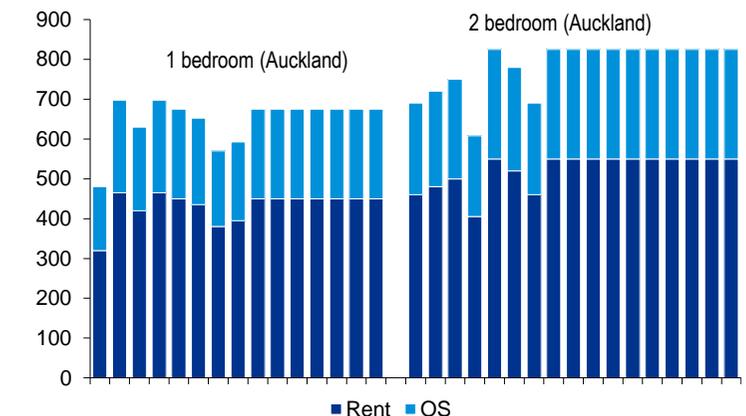
Average OS% across developments (procurement type)

Item	Auckland	RONZ
Build	50%	41%
Turn-key	50%	56%
Direct Leasing	47%	80%
Lease	37%	-
Total	46%	58%

We note that the relatively high value for direct leasing is driven by small number (3) of developments outside of Auckland. We have not investigated the underlying business case for these.

Spread of market rent assumptions

After taking account of the development's assumed market rent and the agreed OS%, there is broad consistency in the revenue per unit across developments. This is a reflection of the assumed rent in Auckland generally being at the maximum allowed by the current rent maxima.



Public Housing government expenditure and value for money

Government expenditure summary (8 of 8)

The lifetime cost to government of OS per unit is approximately \$155k for a 1-bedroom unit and \$194k for a 2-bedroom unit.

After considering Build and Turn-Key units in Auckland only (to achieve a fairer comparison), our dataset suggests the cost to government for these units has been broadly similar across OS and UF for developments to date.

Lifetime cost of OS per unit

The 'whole of life' cost of OS for each development is based on the discounted cost over 25 years. This is based on a real discount rate of 4% per annum, consistent with the Treasury standard discount rate for general purpose office and accommodation buildings. Given the use of a real discount rate, market rent nominal inflation is assumed to be consistent with CPI. Note that the table below is based on HUD's calculations of the whole of life cost of OS, rather than a KPMG calculation.

Table: Whole of life OS cost per unit

Auckland		
Procurement type	1 bedroom	2 bedroom
Build	184,809	213,918
Turn-key	183,962	220,447
Direct Leasing	171,812	209,992
Lease	116,054	176,868
Total	162,783	211,708
Rest of New Zealand		
Build	112,764	120,126
Turn-key	96,727	174,363
Direct Leasing	167,547	213,241
Total	131,470	156,964
Total		
TOTAL	154,954	194,190

Relative cost of UF and OS

The following table provides a summary of the average cost to government per unit under recent UF and OS developments. Our data on UF is for Build and Turn-Key only and does not separate out the development cost by 1 bedroom and 2 bedroom units. It is also predominately Auckland based. We have therefore presented a combined average which implicitly assumes that the mix of 1 and 2 bedroom units between OS and UF developments is the same. Given this, the results are intended to be indicative only.

Average cost (Build and Turn-key, 1-2 bedroom units, Auckland)		
	UF	OS
Whole of life cost	208,492	212,422

broadly similar for projects agreed to date. This is a reflection on the particular assumptions for these projects, rather than a general statement that UF and OS are necessarily of similar cost to the Crown, as discussed earlier in section 2.

There are however other differences that may support a preference for government between OS and UF in particular circumstances. We discuss these in further detail in section 6.

Public Housing government expenditure and value for money

HIF and SHU Funds

This page provides a brief overview of the HIF and SHU Funds that have previously supported the development of new supply for social and affordable housing.

Although available data is limited, HIF and SHU together have supported the development of approximately 300 current IRRS places, with a further 280 units recorded as available for a future potential IRRS contracts.

Housing Innovation Fund (HIF)

The HIF fund was established in 2003 to increase the supply and delivery quality of social housing. It aimed to support low and moderate income households who were not served by the private market, but would be unlikely to be offered a state house, as well as other low income households whose specific housing needs were not being met such as Maori and Pacific groups, or those with mental illness and disabilities.

There were two funding strands to the HIF programme - providing funding to Community Based Organisations (CBOs) in the social housing sector and to local government to support them to grow, retain and enhance their housing stock.

CBO support

Based on an evaluation in 2006, typical HIF Fund arrangements included:

- A conditional grant equating to 15% of the project cost, subject to the property being used as social housing for 10 years; and
- A 25-year loan with the first 10 years being interest free, converting to a table mortgage from year 11 (covering between 44 – 70% of the total estimated project cost). A small number of organisations received suspensory loans (used for social housing for 25 years), where the proposed rent for the property would not be sufficient to repay the loan.

Outcomes

The HIF was disestablished in 2011/12. In summary, a total of \$114.5m allocated in grants and loans were provided to support 1,750 housing units (equating to an average \$65,400 per unit). We note that some conditional grants and suspensory loans were forgiven over the period.

Based on the results of the CHP housing supply survey (Q4 2018):

- 342 properties were marked as being supported by HIF funding (owned or Council lease).
- Of these, 168 had an IRRS status of current contract, potential IRRS contract or unknown. The remaining were marked as not available for IRRS).

Social Housing Unit (SHU) Fund

The SHU fund was established in 2011, administered by the Social Housing Unit. The SHU fund was established to provide capital grants for the development of both affordable and Public Housing. The SHU predated the ability for CHPs to access IRRS. A goal of the SHU was to facilitate the investment of third parties in the supply of social and affordable housing.

Outcomes

Based on information provided to us by MBIE:

- The SHU Fund allocated approximately \$140m of capital grants to 33 CHPs to support 1,011 new social and affordable units.
- On average, the capital grants equate to an average grant of \$138k per unit, or 44% of total project cost.
- As at April 2019, 892 of the 1,011 units have been completed.
- The SHU Fund was not designed to specifically increase the number of IRRS Public Housing settings as these did not exist at the time. Of the 892 completed units:
 - 298 were completed by organisations that predominately provide affordable housing, rather than IRRS housing.
 - 201 are current IRRS places (based on an MSD matching exercise undertaken in March 2017).
 - The remaining 393 units are not currently IRRS places, potentially due to them being tenanted prior to the introduction of IRRS (and therefore may become a Public Housing unit after current tenants no longer require the property). However, the true reason is not known.
- The CHP supply survey records slightly number of SHU units currently under IRRS contract (251), with a further 163 being recorded as being potential IRRS places.

Public Housing government expenditure and value for money HNZ development and sale proceeds

The adjacent table provides a summary of HNZ's development costs and sale proceeds over the last three years.

The data indicates the significant increase in expenditure on developments and acquisitions by HNZ over the period.

HNZ development/acquisition costs and sale proceeds (2016/17 to 2018/19)

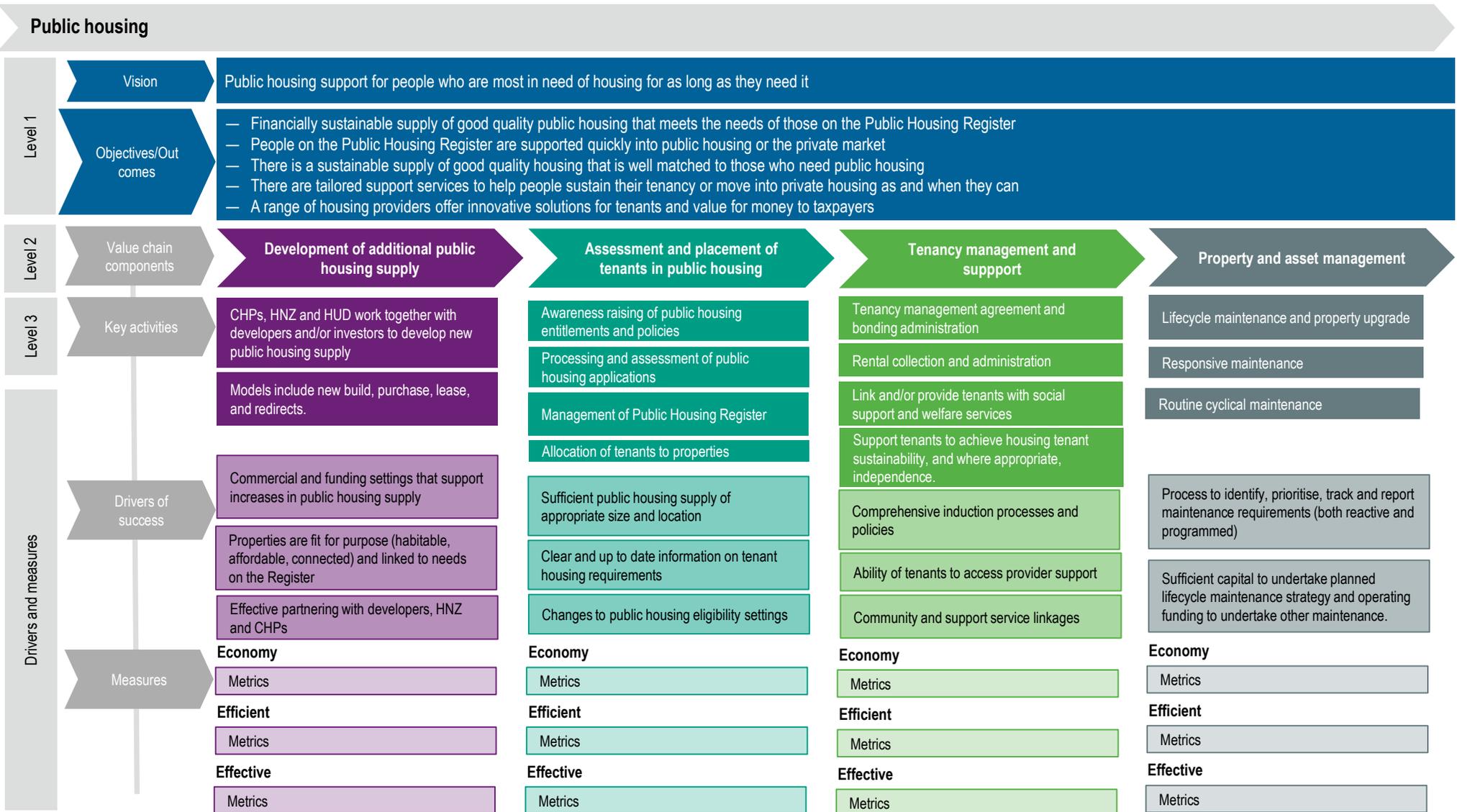
\$m	2018/19	2017/18	2016/17
Additions			
Redevelopments	679.5	410.6	174
New Build Acquisitions	284.8	111.6	20
Buy-ins Units	297.5	230.7	161
Buy-ins Land	8.8	-	-
Capitalised Overhead	31.6	9.8	2
Total HNZ Additions	1,302.3	762.7	357
Affordable / Open Market Units	181.3	4.6	-
McLennan Development	9.6	8.1	25
Total non-HNZ Additions	190.9	12.7	25
TOTAL Additions	1,493.2	775.4	382
Proceeds			
General Sales	(22.5)	(19.5)	(63)
Affordable/Market Sales	(85.2)	(1.7)	
McLennan Land Sales	(18.6)	-	(45)
Vacant Land Sales	(4.4)	(16.5)	
TOTAL Proceeds	(130.6)	(37.8)	(108)
Net Capital Expenditure	1,362.6	737.6	274

Public Housing government expenditure and value for money

Value for money framework

Introduction

The following diagram provides a framework for considering the different components and activities of the supply of Public Housing. Within each component, we consider the evidence on key economy, efficiency and effectiveness metrics.



Public Housing government expenditure and value for money

VfM: Development of additional Public Housing Supply (1 of 2)

HNZ achieved its revised target for FY19 delivery of new supply through the delivery of a significant number of new units in the final month of the period.

We understand that HNZ is continuing to refine its approach to phasing of monthly budgets and delivery time information.

Introduction

For the purpose of considering value in the growth of new supply, we have focused on available evidence across three metrics:

- **Economy:** The cost of new supply units incurred by providers. This is discussed in section 1.
- **Efficiency:** The level of government subsidy incurred by the government to support new supply. This is discussed earlier in this section.
- **Effectiveness:** The track record of new supply delivery.

Effectiveness: Track record of delivery

HNZ met its revised target for new supply in FY19, representing a significant increase on delivery relative to previous years

HNZ achieved its revised internal budget for the delivery of new supply in FY19, through the delivery of a significant number of units in the final month of the year. While HNZ did revise its internal targets down during the year, we understand these represent 'stretch' targets for internal measurement only. We have not considered the reasonableness of HNZ's targets.

Table: HNZ delivery of new Public Housing supply (actual)

Homes delivered - July 2016 to June 2019 (quarterly)															
Number of units	Sep-16	Dec-16	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	FY17	FY18	FY19
Redevelopment	41	65	61	188	32	111	68	471	41	179	200	620	355	682	1,040
Turn-key	10	18	5	21	12	27	29	88	40	50	43	288	54	156	421
Buy-in	16	21	67	126	50	53	45	101	86	83	74	159	230	249	402
New leases and renewals	75	131	120	145	213	243	222	119	0	105	0	0	471	797	105
Total additions	142	235	253	480	307	434	364	779	167	417	317	1067	1,110	1,884	1,968
Demolitions (redevelopments)	(86)	(76)	(118)	(207)	(135)	(100)	(47)	(119)	(46)	(112)	(250)	(144)	(487)	(401)	(552)
Leases expired	(95)	(165)	(164)	(183)	(257)	(284)	(256)	(147)	(37)	(19)	(27)	(36)	(607)	(944)	(119)
Sales	(136)	(93)	(52)	(14)	(15)	(20)	(17)	(18)	(17)	(9)	(8)	(20)	(295)	(70)	(54)
State House transfers	-	-	-	-	-	-	(3)	(7)	-	-	-	(6)	-	(10)	(6)
Total disposals	(317)	(334)	(334)	(404)	(407)	(404)	(323)	(291)	(100)	(140)	(285)	(206)	(1,389)	(1,425)	(731)
Adjustments	-	-	-	-	-	-	-	-	4	6	2	(26)	-	-	(14)
Net increase / (decrease)	(175)	(99)	(81)	76	(100)	30	41	488	71	283	34	835	(279)	459	1,223

The June uplift is partially the result of how HNZ report and forecast new supply delivered throughout the year

We understand that the June uplift in delivery is partially a reflection of earlier monthly actual results not necessarily counting all units during the year. This is due to the difficulty and time required in applying the delivery definition throughout the year for some properties. During the year, the monthly results count houses handed over (or 10 day notice issued), with the June month also capturing houses delivered earlier in the year that meet the HNZ's agreed delivery definition. For example, some properties can be considered delivered if final CCC completion has been undertaken but not all the documentation is complete, or where the Construction Group manager believes a property should be included and this has been authorised in writing by HNZ's Chief Financial Officer.

HNZ is developing its tracking of delivery times

We discussed with HNZ the availability of data on the delivery times for new developments (for example, a dataset setting out project start, proposed construction start/end date, actual construction start/end date).

Data from HNZ on these metrics were not available as part of this review, but we understand that HNZ is developing measurement in this area.

Public Housing government expenditure and value for money

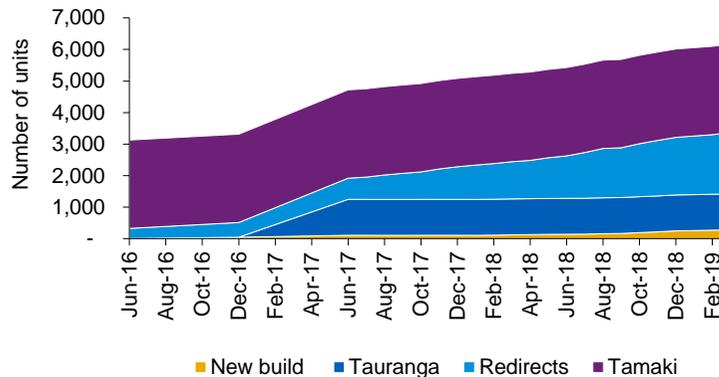
VfM: Development of additional Public Housing Supply (2 of 2)

Recent new supply from CHPs has been largely provided through redirect properties and the result of HNZ property transfers. However, CHPs are continuing to build capability in new developments with 1,103 (contracted and approved) properties in the pipeline.

Effectiveness: Track record of delivery (cont.)

The vast majority of new Public Housing supply has been achieved through redirects of existing properties or the result of the previous transfers of HNZ properties.

Diagram: CHP additional supply over time



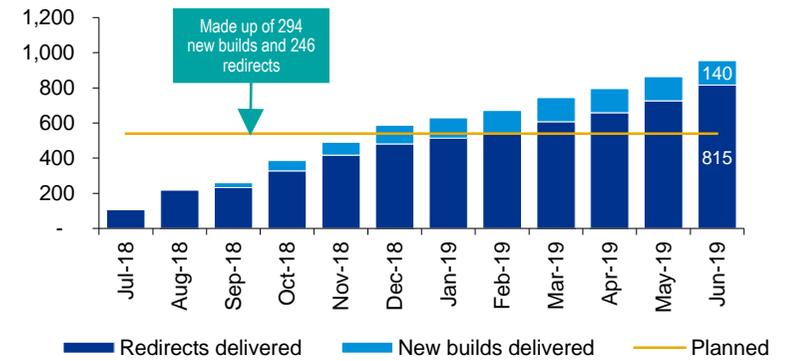
The tracking of CHP supply delivery against a target is also relatively recent

While the FPDG tracks developments on an ongoing basis, the tracking of CHP delivery against a 'target' is relatively new. Changes in funding policy settings and procurement definitions also mean that historic time series lack comparability to allow conclusions to be drawn.

In 2018/19, CHPs exceeded the planned target for the year, although the bulk of new supply is still redirects

As shown in the graph on the right, the delivery of new units for CHPs exceeded the overall target.

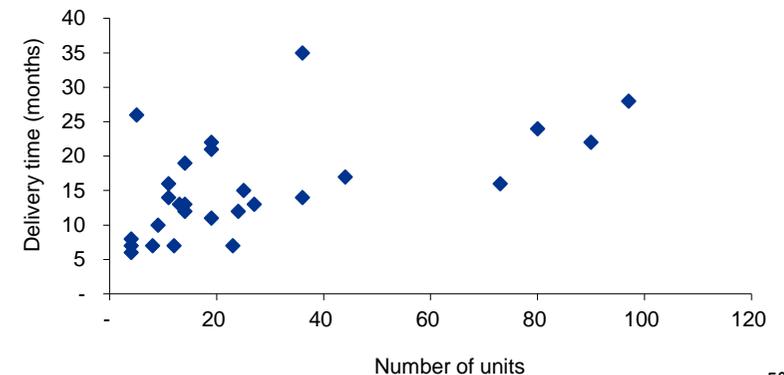
Diagram: 2018/19 CHP target vs. actual delivery



At the time of this report, we understand that there are a further 1,103 properties in the pipeline (contracted and approved), with 667 still to be procured through the market. HUD expects that the CHP delivery target set out in the Public Housing Plan will be met.

Diagram: Estimated construction times for CHP developments

The following graph provides an measure of delivery times for developments based on construction start and end dates. This should be considered indicative only due to potentially variable data quality.



Public Housing government expenditure and value for money

VfM: Assessment and placement of tenants in public housing

We have not focused on the assessment and placement of tenants in Public Housing in detail. The data highlights the well-known issues of the growth of the Public Housing Register and the challenge HNZ faces in matching its historic portfolio to modern tenant cohort needs.

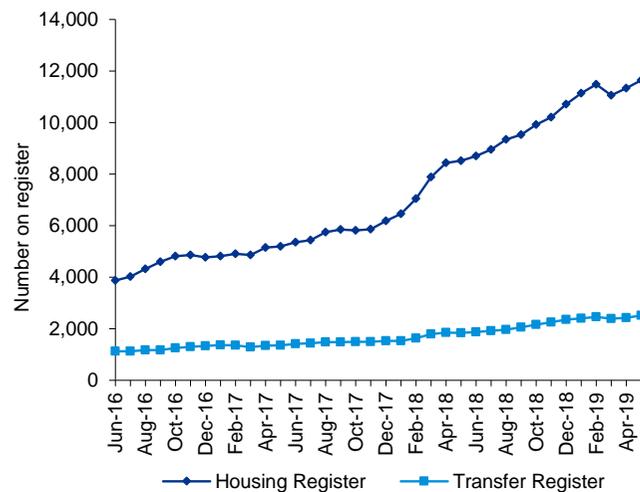
Introduction

For the purpose of this component of the value chain, we only focused on two metrics related to this value chain component:

- **Effectiveness:** Size of the Public Housing Register
- **Effectiveness:** Tenant matching

Effectiveness: Size of the Public Housing Register

The Public Housing Register has grown significantly....



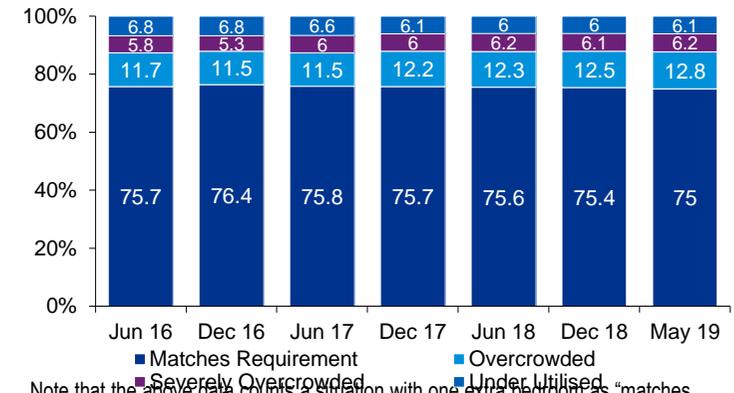
...which highlights the importance of CHPs and HNZ bringing on new Public Housing supply.

The Public Housing Plan includes a target of 6,400 places by 2021/22 through HNZ (4,480 places) and CHPs (1,920). We understand that there is no official forecast of the Public Housing register over time, but HNZ includes a long-term supply scenario in its LTIP as maintaining its existing market share of the national market.

Effectiveness: Tenant matching

The level of tenant matching is relatively low for the existing HNZ housing stock, representing the change in tenant cohort since the stock was developed...

There is a current misalignment between HNZ's existing stock and those of tenant needs, reflecting the shift towards sole parents with children and single person households, which are less suited to three-bedroom houses which make up approximately 40% of HNZ's portfolio.



Note that the above data counts a situation with one extra bedroom as "matches requirement", with two or more extra as "under utilised".

...although this metric has some limitations in assessing portfolio management

While the metric does provide an indication of stock realignment, there may be legitimate reasons for tenants to prefer a larger house than a bedroom match metric might indicate. HNZ also has limited tools to improve matching of existing tenants in the short-term, given the lead-time in changing the composition of its portfolio.

There isn't similar data available for the CHP sector

There is not similar easily accessible information for the CHP sector, although we understand that MSD does hold some data that, with further preparation, could be used for tenant matching analysis in the future.

Public Housing government expenditure and value for money

VfM: Tenancy management and support (1 of 4)

Tenancy management and support are key functions of a Public Housing provider given the needs of tenants are generally greater than those of the general renting population.

Prior to considering quantitative measures relating to tenancy management, we have summarised responses from a survey of the CHP sector we conducted in June 2019.

Introduction

For the purpose of considering value in tenancy management and support, we have focused on available evidence across key three metrics:

- **Economy:** Tenancy management and staff costs
- **Efficiency:** Tenancy management service levels
- **Effectiveness:** Tenant satisfaction measures

Prior to discussing these, we provide a summary of qualitative feedback received on tenant cohort and tenancy management received in our survey of the CHP sector.

CHP survey results: Tenant cohorts and management

Characteristics of tenant cohort

Our responses were from a range of CHPs, the majority of which indicated a specialisation of tenants, such as mental health or the elderly. The description of tenants provides insight into potential tenant management challenges, over and above those of a typical market rental. For example, these include:

- Complex physical and mental health needs, as well as tenants that suffer from loneliness and social isolation.
- Preferences and/or requirements on location, such as being near health providers or not in mixed tenure developments (i.e. preferring not to live amongst families and young people).
- Recent migrants that may have limited English skills, or other tenants that face cultural barriers in the general rental market.
- A vulnerability to homelessness, such that sustaining a long-term tenancy is challenging.

We note from CHA's supply survey that CHPs (across their entire portfolios, not only IRRS) indicate key target groups of elderly/kaumātua (23%), low income families (10%) and people with disabilities (8%). 51% of properties did not have a recorded target group.

Tenancy management service

The survey sought responses on the types of tenancy management services over and above those of a conventional landlord. A summary of these services include:

- Referrals of wrap-around services, such as health services, budget services, community support agencies (such as Age Concern) and employment services.
- Support with day to day activities, such as setting up televisions, internet service and arranging social activities, and practical household management.
- Budgeting advice and support, such as agreeing to savings and debt repayment goals, accompanied by regular check-ins.
- Support and advocacy on behalf of tenants for negotiating and discussing with utilities and other services.
- The provision of tenant meals (e.g. two cooked meals), with the benefit of further social contact with socially isolated tenants.
- Welfare inspections, often undertaken as part of regular property inspections.

The results indicate that there is generally no difference in the tenancy management service offered to the CHPs' affordable and Public Housing tenants. However, some CHPs indicated that Public Housing tenants can be more demanding on staff time and that, where a household has a frequent change of income (with corresponding change in IRR), this can result in rent arrears issues. A delay in MSD providing this information to the CHP was also cited as an issue by one CHP, although we understand MSD does not recalculate IRR unless the change in income is perceived to be permanent.

While the above data does provide qualitative information on services, there is no systematic categorisation of service levels that would allow a quantitative measure of comparative service levels between CHPs. There has been no historic requirement through contract or regulation for this.

Public Housing government expenditure and value for money

VfM: Tenancy management and support (2 of 4)

The available data considered in section 2 indicated that tenancy management costs are broadly in line with international benchmarks.

Economy: Tenancy management staff and costs

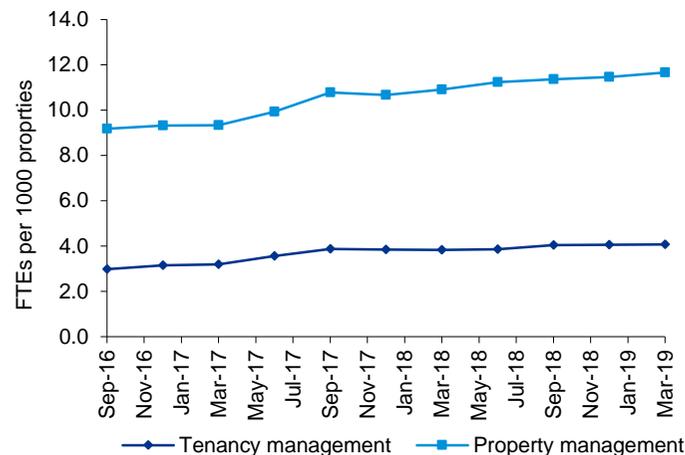
Our analysis in section 1 indicated a variation in tenancy management costs between HNZ and CHPs for new supply...

Our analysis in section 2 indicated HNZ's tenancy management costs were higher than those of the CHP sample, but we note caution given the limited sample of CHP data and the significantly different business models (as seen by HNZ's corporate overhead component). The analysis also indicated these were broadly in line with international benchmarks.

The number of HNZ tenancy management FTEs per 1000 properties has increased over the last three years.

HNZ has a significantly different business model than any of the CHPs, driven by its significant size and need to serve a diverse tenant base. We note that HNZ is currently trialling an intensive tenancy management programme which is partially driving increased costs for tenancy management.

Diagram: HNZ tenancy and property mgmt. FTEs per 1000 properties



The quantitative information on CHP costs collected in the CHP survey shows significant variability.

We asked CHPs to indicate the number of properties within their portfolio and the total tenancy management costs on an annual basis. The information received from the 16 responses is patchy with highly variable results, and we would caution placing significant weight on the numbers.

In particular, tenant manager FTE per 1000 properties is not generally meaningful given the small portfolios of CHPs. The survey sought to separate property administration from tenancy management, although the data provided does not allow us provide meaningful property management results.

Table: CHP survey results (tenancy management)

CHP*	Units	Total TM cost (\$m)	TM cost per unit (\$)	Total TM FTEs
CHP 1	250	1.013	4000	9.3
CHP 2	2185	3.2	1464	15.5
CHP 3	1828	N/A	-	9.7
CHP 4	6	N/A	-	0.5
CHP 5	290	12% of rental income	-	3
CHP 6	74	0.133	1797	1
CHP 7	45	0.054	1200	0.65
CHP 8	135	0.216	1600	2
CHP 9	161	Volunteers	-	Volunteers
CHP 10	251	0.177	705	2.5

* The CHP numbering across this section is not intended to be consistent (i.e. CHP 1 is not the same CHP across data tables)

Public Housing government expenditure and value for money

VfM: Tenancy management and support (3 of 4)

The measurement of the efficiency of tenancy management is limited by our lack of defined service levels by different providers. We comment on this further in our discussion of benchmarking in section 5.

Efficiency: Tenant management service levels per cost unit

The level of service provided to tenants is not systematically measured at present, which makes efficiency comparisons across providers challenging...

There is no consistent methodology to consider the different levels of service provided by different providers, for example, between core tenancy management, linking tenants with broader service, and directly providing services to tenants. The broad spectrum of tenancy management services is understood at a high level, but there is no sector-wide methodology to classify particular services into standard groupings. The outcome of this is that measuring the efficiency of delivery (i.e. the extent to which higher or lower costs can be explained by differences in service levels) cannot be undertaken given current data limits.

...but there are sector reporting approaches that could be adopted in the future to develop this area of performance measurement

There are existing approaches to the categorisation of tenancy management services that could support the measurement of efficiency. We discuss these issues in greater depth in section 5 on benchmarking.

Effectiveness: Tenant satisfaction measures

The measurement of tenant satisfaction is a key measure of tenancy management performance used internationally...

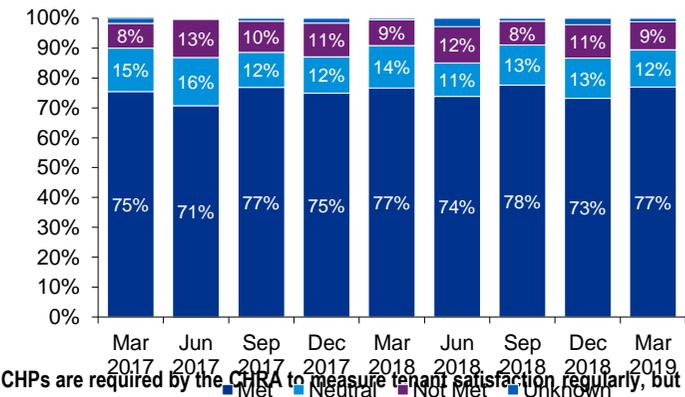
The surveying of tenants to measure their satisfaction with their home and the services received from their provider is a standard measure of the quality of tenant management.

A key limitation in comparing results between providers is the lack of a standard surveying methodology (i.e. consistent style questions, approach to soliciting responses from tenants etc). While this does create the risk of invalid comparisons, our review of international benchmarks is that a standard of around 85% satisfaction is common for Public Housing tenants.

A limitation of overall tenant satisfaction measures is that they do not necessarily capture other services that a provider could be delivering to tenants that tenants may not be aware that they would benefit from, or that may be offered by other providers.

HNZ tracks a number of tenant satisfaction measures through a customer survey - the majority of tenants indicate an overall satisfaction with HNZ's services

Diagram: HNZ overall tenant satisfaction



CHPs are required by the CHRA to measure tenant satisfaction regularly, but there is no regular centralised process to report and analyse this data.

As part of its 2018/19 annual monitoring process, CHRA had a particular focus on tenancy management, including tenant complaints and tenant surveys. This information however is not available on a consolidated or standardised basis for data analysis.

For those that did provide results through the survey undertaken for this report, almost all of the CHPs reported overall tenant satisfaction scores of around 90-100% or other qualitative descriptors indicating 'high' results. We do not however have any insight into the robustness of the methodologies used.

Public Housing government expenditure and value for money

VfM: Tenancy management and support (4 of 4)

The second tenancy management effectiveness domain is tenant sustainability. HNZ data provides a reasonably detailed breakdown of tenant exit reason, although our CHP data is limited to the % of tenancies sustained over time periods.

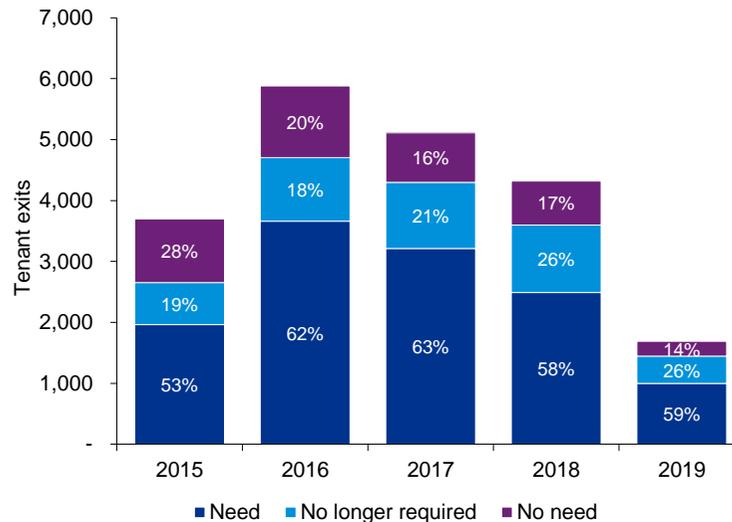
Effectiveness: Tenant sustainability and exits

A key role for a Public Housing provider is to support tenants to maintain their tenancy...

This can involve working with tenants more intensively as required to prevent a tenancy being terminated by ensuring the tenant is meeting their obligations. This can be measured through both tenant sustainability measures (i.e. proportion of tenancies still active after particular time periods) and measuring 'adverse' exits (i.e. exits from the tenancy where a housing need still exists)

HNZ data indicates that a housing need still exists in a relatively high proportion of tenant exits

The classification of need is based on an HNZ mapping of tenant exit reasons. Examples where a housing need still exists include cases where the tenancy has been terminated, abandoned by the tenant or where the tenant has chosen to move to be closer to support, friends and family.



Note: "No longer required" includes exit reasons such as the tenant moving to a rest home or hospice. "No need" includes exit reasons such as tenant choice to exit (shift to private sector) and termination following an MSD review.

Based on a categorisation of tenant exits where a need still exists, approximately 40% are coded as "Other – tenant choice", while 16% are due to "personal safety", and a further 16% is due to "Closer to support – tenant choice".

Without a readily available comparable external benchmark, a decreasing proportion of such exits over time could be used to measure positive progress on this metric.

Data from the CHP survey on tenant sustainability from the CHP survey is patchy. It broadly indicates relatively high sustainability, but also a likely lack of data measurement by CHPs

Tenant sustainability

Broadly, CHP responses indicated that between 90-100% of tenancies are sustained in the first year, with a few CHPs recording sustainability of 100% or close to it.

- A couple of CHPs reported tenancy sustainability rates of closer to 75%-85%. We note that the lower results were reported in surveys that were completed in more detail, which may indicate the slightly lower rates may be more reliable.
- Broadly, the CHP responses indicated a 3-year tenant sustainability rate of around 70%, although the response to this question was patchy with a range of 25% to 99%.

Tenant exits

- The results do not allow reliable comparisons between providers, particularly given the small sample of data and small number of tenants (e.g. less than five exits in a year). Very few responses included detail on this question, and there is no common coding system for recording tenant exit reason within the sector.
- For exits that were described, the reasons cited included tenant death, private rental or higher level of care and eviction (e.g. rent arrears, methamphetamine, anti-social behaviour).

Public Housing government expenditure and value for money

VfM: Property and asset management (1 of 4)

Our value assessment of property and asset management is based on five metrics covering both the management of properties by the provider and the tenant's experience of their home.

Introduction

The effective management of a property ideally requires a strategic approach to reactive and planned maintenance, as well as capital replacement over the property's lifecycle. With an effective asset management approach, the provider is able to maintain the capital value and market rent of the property, as well as contribute to tenant satisfaction through a healthy and dry home.

For the purpose of considering value in property and asset management, we have focused on available evidence across five metrics. These are intended to cover both the provider and tenant perspectives on property management.

- **Economy:** Cost of repairs and maintenance per property.
- **Efficiency:** Proportion of repairs and maintenance on planned activity.
- **Effectiveness:** Average completion time for various repairs and maintenance works.
- **Effectiveness:** Average 'turnaround' time.
- **Effectiveness:** Tenant satisfaction measures (maintenance service, home satisfaction, warm and dry).

Economy: Cost of repairs and maintenance per property

The level of repairs and maintenance required by a property depends on the age, size and condition of the property.

As previously discussed, HNZ's estimated repairs and maintenance costs differ by unit age and typology. Given the differences in portfolio age, quality, and build style, direct comparisons of cost per unit should be interpreted carefully. In addition to the benchmarks set out on in section 2, previous KPMG analysis considered further benchmarks for the per unit cost of repairs and maintenance.

For reference, HNZ's estimated repairs and maintenance cost per unit (excl. capital replacement) for a 3 bedroom house is between \$4000 and \$4870 per annum (depending on the age of the property).

	Responsive repairs	Cyclical maintenance	Major works	Total
AM consultancy forecast	Not included	\$4,200		\$4,200 + responsive
Normative analysis	\$936	\$0 - \$625	\$1,441 - \$2,494	\$2,377 - \$4,057
UK benchmark*	\$790 - 821	\$390 - \$442	\$1,200 - \$2, 258	\$2,463 - \$3,438

The data for the CHP sector is of generally patchy quality and is not systematically collected

As part of the CHP survey, we asked for data on total property management costs, with the results summarised below. We have removed entries with implausible results.

CHP	Units	Total R&M cost (\$m)	R&M cost per unit (\$)
CHP 1	251	1.674	837
CHP 2	290	-	1,750
CHP 3	1692	5.363	2,682
CHP 4	66	-	2,800
CHP 5	2162	4.06	2,030

* As noted earlier, UK property coat benchmarks will be impacted by differences in construction industry costs and different building styles with NZ.

Public Housing government expenditure and value for money

Property and asset management (2 of 4)

The data suggests HNZ has a reasonably high level of planned maintenance as a proportion of total maintenance. Similarly, data indicates HNZ now generally meets its responsive maintenance response time targets, although not exclusively.

Efficiency: Proportion of planned repairs and maintenance

HNZ's proportion of planned to responsive maintenance appears consistent with benchmarks.

The strategic planning of property maintenance should result in a relatively high proportion of maintenance spend being planned. It would also generally be expected to be less costly than responsive work (e.g. fewer urgent callouts).

The following table provides a summary of available data for HNZ, a small number of CHPs and available international benchmarks. A higher result is considered generally preferable, although there are property components that are most efficiently run to failure (i.e. a result of 100% would never be expected).

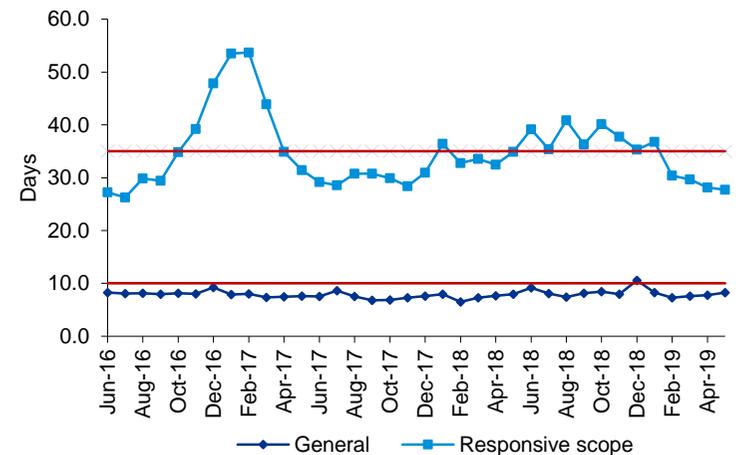
	Planned repairs and maintenance as a proportion of total
HNZ (16/17 – 17/18)	68 – 71%
Sector scorecard 2018 (UK)	Higher Quartile: 69% Median: 62% Lower Quartile: 53%
CHP 1	71%
CHP 2	61%
CHP 3	42%

Efficiency: Average completion time for repairs and maintenance

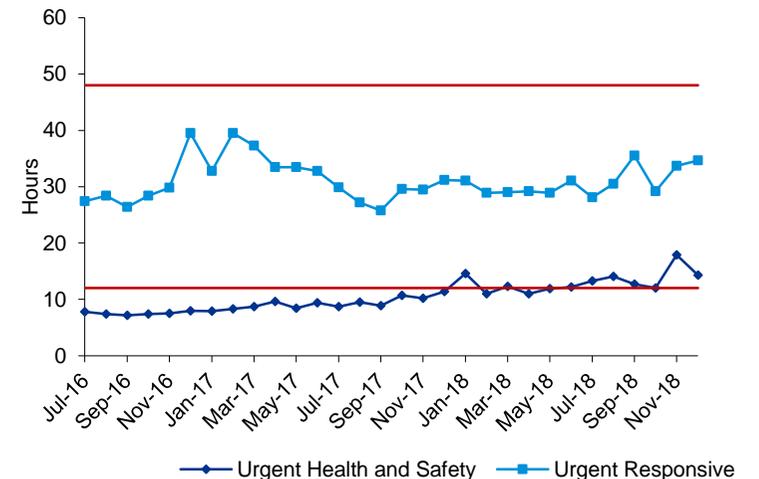
HNZ targets 10 days and 35 days to complete general responsive work orders and responsive scope work orders respectively...

HNZ classify non-urgent repairs and maintenance work as general and responsive scope (larger defects or follow on work after a temporary repair).

There is a limitation in only considering an average (i.e. negative outliers are not visible), but available data suggests a reasonable level of compliance against the performance standard.



...and between 12-48 hours for completion of urgent responsive and health and safety issues



Public Housing government expenditure and value for money

Property and asset management (3 of 4)

The data from the CHP survey demonstrates a range of response times for different maintenance requests. We would suggest similar caution as for other results from the survey.

Effectiveness: Average completion time for repairs and maintenance works (cont.)

The CHP sector has varied response targets for repairs and maintenance, and available data is very patchy.

We sought response time data from CHPs for general responsive and health and safety issues. In general, it appears that target times were provided through the survey rather than actual response time data. A further caveat is that there is likely to be difference in how the question was interpreted across different CHPs e.g. response time vs. completion time, definition of a “general” and “health and safety” response.

	General responsive	Urgent H&S responsive
CHP 1	Typically a day	Typically a couple of hours
CHP 2	2-3 days	Same day
CHP 3	3 days	2 hours
CHP 4	Emergency: <1 day Urgent: 2 days Standard: 12 days	Same working day
CHP 5	1 day	-
CHP 6	Urgent: 7 days General: 4 weeks	4 hours
CHP 7	10 days	4 hours
CHP 8	10 hours	3 hours

Effectiveness: Turnaround time

The ‘turnaround time’ between a tenant vacating a property and the property being ready to let is a common property management performance measure. The interpretation of turnaround time does require some caution, as a slow turnaround time for any particular property may be due to renovation between tenancies or other reasons not reflective of performance. Similarly, there may be no fiscal impact on the Crown from a longer turnaround time if the property is part of an open term agreement that ends as soon as the previous tenancy ends. However, this does represent a reduction in supply when the property is sitting vacant.

	Average days from a property becoming vacant to being ready to let
HNZ (2016)	29.3 days
HNZ (2017)	19.3 days
HNZ (2018)	16.2 days
CHP 1	1 week
CHP 2	20 – 30 days (CHP noted meth decontamination issues)
CHP 3	3 -7 days
CHP 4	3 days
CHP 5	40 days
CHP 6	10.5 days

Public Housing government expenditure and value for money

Property and asset management (4 of 4)

Another perspective on property management performance is tenant satisfaction with the house and the maintenance service they receive. The data on the CHP sector is again limited, and therefore would caution against direct comparisons with HNZ.

Effectiveness: Tenant satisfaction measures relating to repairs and maintenance and asset condition

Diagram: Overall satisfaction with HNZ home

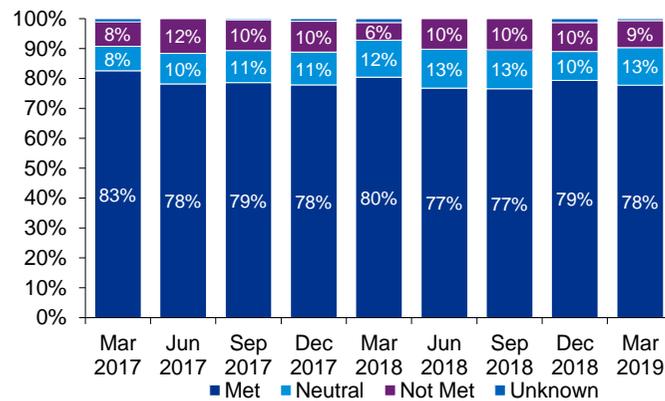
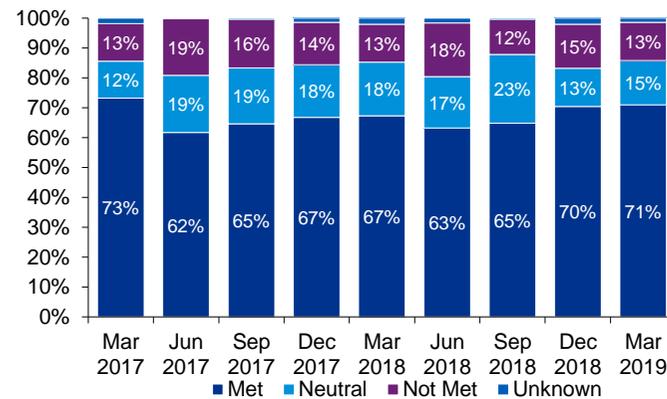
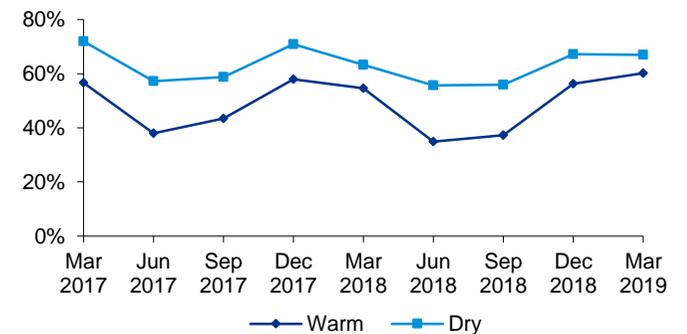


Diagram: Overall satisfaction with repairs and maintenance provided by HNZ



Overall Satisfaction their home is warm and dry



CHPs generally reported high levels of tenant satisfaction with their homes and the repairs and maintenance service they receive, but we caution against any direct comparisons with HNZ data

CHP property management satisfaction		
	Overall satisfaction	R&M service satisfaction
CHP 1	High	High
CHP 2	96%	96%
CHP 3	92%	86%
CHP 4	90%	85 – 90%
CHP 5	65%	73%
CHP 6	100%	97%

Public Housing government expenditure and value for money

Further observations

While the current sector wide analysis on value for money is still relatively limited, the exercise has been valuable in providing an initial stocktake and understanding data gaps and limitations.

Comment

The preceding analysis has provided a summary value for money analysis based on available data. It represents an step towards improving understanding of service levels, costs and performance across the sector. Our broader observations from this exercise are below.

The sector is characterised by a large data-rich provider and a significant number of much smaller providers of which there has historically not been significant systematic data collection

From a data perspective, there is a significant asymmetry to what is readily accessible from HNZ relative to the CHP sector. The new CHP contracting framework requires additional data reporting, including on occupancy, tenancy churn, exit reasons, repairs and maintenance response times and tenant satisfaction measures. This will represent a significant step-forward, although we would also support, over time, further consideration of measuring service levels and costs (see section 5 for further discussion).

Some CHPs appear to not collect or have access to the types of data requested in the CHP survey

The level of quantitative information provided from those CHPs that responded was relatively limited, either not providing the information at all or only providing a single year of data. Although we note that, in some cases, the CHP may only have been operational for a relatively short period of time. Further, it should be noted that the survey was provided to CHPs with limited advance notice and a requested response time of 3 weeks.

It does however suggest that some CHPs may not use performance metrics as a means to support their operations. Some of the comments on the availability of data include:

- The CHP does not hold the data or the performance metric is not measured by the CHP

- The information is managed locally, with no centralised records
- In most cases, no reason was given for the information not being provided (i.e. template was blank)

The 'value add' of the CHP sector is challenging to measure given current data limitations

A key potential benefit from a diverse CHP sector is the specialisation of tenancy management from smaller local organisations that have experience in meeting the needs of particular tenant cohorts. It potentially provides a degree of competitive tension and incentives for HNZ performance beyond its regular accountability arrangements. In addition, CHPs may be willing to deliver Public Housing supply in areas where HNZ does not currently have plans, including with support of private sector capital.

However, it is currently difficult to evidence these from a data perspective given CHPs have not been historically required to collect and report performance and cost information.

While the current data limits the comparability of different parts of the sector, there is benefit to moving towards a consistent benchmarking framework

We largely agree with provider concerns that existing data does not sufficiently account for differences such as business models, tenant cohorts and provider size. Given that, comparisons between providers can only be considered indicative given data limitations. As we discuss in section 5, we see benefit in moving towards being able to more robustly compare cost and performance across providers.

4

HNZ's stock reconfiguration and maintenance plans

HNZ's stock reconfiguration and maintenance plans

Summary

At the time of this review, HNZ is currently updating its LTIP through discussions with its Board, HUD and the Minister.

While we have been provided with draft numbers, we have not presented these here as they are subject to further change.

Introduction

HNZ has a significant portfolio of existing assets. In managing its portfolio, HNZ is balancing the provision of positive social outcomes by meeting the needs of the current and prospective tenants on the Public Housing Register and supporting its own long-term financial solvency.

HNZ's strategic framework includes key strategies that set out HNZ's plans and programmes:

- **Long-term Investment Plan:** balances trade-offs to deliver a financially sustainable investment plan over the next 30 years.
- **Asset Management Strategy:** Asset Management goals, settings, strategic options and levels of service
- **Housing Investment Framework:** Targeted financial outcomes for the portfolio
- **Regional Investment Plan:** HNZ's proposed delivery plan for regional New Zealand.

Summary

The draft LTIP is still a work in progress and is being developed by HNZ. Given this, we have not sought to include a discussion of numbers from the draft as these are subject to further change, internal HNZ discussion and refinement.

Broadly, the draft LTIP is divided into three segments:

1. **Running and improving HNZ's existing portfolio:** This would be achieved through ongoing maintenance of existing homes, upgrading and retrofitting homes that reach the end of their economic life and realigning homes to be in the right place with the right typology.

2. **Growth of the Public Housing portfolio :** This includes a number of in stacked initiatives, from meeting the current Public Housing Plan target of 4,480 new homes, with options for additional refugee housing, transitional housing and, most significantly, HNZ maintaining its existing market share of 3.6%.
3. **Community development:** This includes HNZ playing a significant role in developing private affordable homes and Kiwibuild homes, including community amenity and infrastructure development.

Comment

- The draft LTIP and supporting financial models appears to be a significant advance on the previous LTIP in making clear the trade-offs between maintaining and upgrading its existing portfolio and the delivery of new supply. We support the continued evolution of the LTIP as a valuable tool for HNZ, HUD and Ministers. We have not commented on the specific numbers and scenarios as these are still a work in progress.
- HNZ has numerous levers which can have an impact on the cost of delivering components in the LTIP. For example, the extent of retrofitting older homes for thermal performance, poor layout and redecoration. For all these levers, there is benefit from ensuring that decision making responsibility and consultation requirements are clear (i.e. HNZ Board, HNZ operational decision, level of HUD and Ministerial consultation and direction).

5

Public Housing Benchmarking

Benchmarking Introduction

This section summarises the literature on effective benchmarking in Public Housing and suggests a potential way forward to improve cost and performance benchmarking.

Introduction and scope

Our work to better understand cost and performance in Public Housing has highlighted the challenges in drawing firm conclusions from existing data. As outlined earlier, these include a current lack of:

- accessible data on cost and performance in the CHP sector.
- a consistent framework for capturing cost data across the sector.
- a consistent framework for the description of services levels and performance across providers (taking account of organisational and methodological differences).

We consider there is further work required before robust benchmarking can be undertaken in the sector.

Given this, this section covers:

- the purpose and principles of benchmarking.
- the key sector-specific challenges in effective benchmarking in Public Housing.
- international examples of cost and performance benchmarking in Public Housing.
- approaches to managing the challenges of effective benchmarking in Public Housing.
- potential next steps that HUD could undertake to progress robust benchmarking for Public Housing.
- potential benchmarking metrics for Public Housing.

Purpose of benchmarking

Benchmarking is the practice of comparing cost and performance metrics against peer organisations, international standards, similar programmes in other sectors, specific service standards/targets or across time periods. The potential benefits of effective benchmarking include:

- Consistently assess relative costs, outputs and outcomes in different parts of the Public Housing sector to inform policy and purchasing decisions.
- Provide a signal to providers on the level of costs and performance expected by the purchasing agency.
- Provide data and tools for providers to use to compare themselves against peer organisations and identify improvement opportunities.

Principles of effective benchmarking

At a high-level, we consider the general principles of effective benchmarking metrics to support 'like with like' comparisons include:

- **Attributable** – provider should be plausibly able to influence the metric (e.g. limited value in comparing council rates between providers).
- **Relevant** – the metric should align with desired objectives.
- **Accurate and clearly defined** – the metric should be able to be measured accurately and objectively.
- **Manageable administrative burden and cost** – the collection and analysis of data should be proportional given benefit and intended use.
- **Repeatable** – the process can be repeated without undue cost (i.e. not a single one-off exercise).
- **Understandable** – the metrics and relevance of results should be understandable to decision makers.
- **Contextualised** – where differences between providers cannot be captured by the metric, results should be appropriately contextualised.

Benchmarking

Key challenges in developing comparable Public Housing benchmarks

A key risk in benchmarking is that data is not considered genuinely comparable because it does not account for the 'true' driver of the result.

In Public Housing, some of these potential factors include different service levels, tenant cohort needs, regions and housing stocks between providers.

Key challenges in developing comparable benchmarks

A key principle for effective benchmarking is that factors that may be influencing results are appropriately accounted for in the benchmark design. There will be genuine differences between providers that need to be considered of to ensure that results are not discounted on the basis that a particular unaccounted factor is the true driver of any outcome. In summary, benchmarking should provide insight by disaggregating:

- results driven by deliberate decisions by the organisation (i.e. to provide a particular service quality or target a particular cohort);
- results driven by factors external to the organisation (e.g. regional differences); and
- results that may be due to inefficiency or genuine performance difference, and therefore warrant further investigation.

Public Housing-specific factors

Tenancy management service levels

There are differences in the level of tenancy management services provided to tenants, particularly the extent to which 'enhanced' services are provided over and above those of a conventional landlord. For example, this may involve providing meals to tenants, budgeting and employment advice or additional visits. Without a reasonable understanding of different service levels, a comparison of tenancy management costs per tenant would not on its own provide insight into the relative efficiency of providers.

Tenant cohort

There will be differences in tenancy management requirements driven by the needs of specific tenant cohorts. For example, tenants with mental health issues, a cohort that many CHPs specialise in, are likely to have different needs from the general rental population.

Housing age and standards

The age of the Public Housing stock of different providers will be a driver of provider costs, particularly the cost of repairs and maintenance and capital replacement. The cost per unit for a provider managing a largely new portfolio would be expected to be lower than that of a provider managing a largely aged portfolio.

Cost allocation and methodological differences

There is not a consistent financial reporting framework and set of definitions for the allocation of costs across the sector. For example, the allocation of overheads to particular activities and the treatment of office and lease costs. Tenant satisfaction surveys are also not undertaken using a consistent methodology across the sector.

Operating models and scale

The provider landscape is characterised by a dominant provider, and a large number of smaller CHPs with comparatively small portfolios. These organisations may have significantly different business models and obligations, including, in many cases, providing a range of services in addition to Public Housing. Further, some CHPs may also have a charitable/volunteer dimension that may not be captured in a standard analysis of costs. Finally, some metrics (e.g. FTEs per 1000 properties) will not be meaningful for providers with only a small number of properties.

Organisational maturity and systems

The capacity and capability of small CHPs to collect data for benchmarking may be challenging. For example, activities may be undertaken by volunteers, records may not be kept centrally or systems are not in place to capture the necessary data for benchmarking. The incremental cost of requiring such collection may be significant.

Regional costs

There may be differences in cost driven by the region in which the provider operates in e.g. higher staff salaries.

Benchmarking

International examples (1 of 2)

Housemark are a benchmarking firm operating in the UK. In addition to providing services to housing providers, it also produces the publicly available annual Sector Scorecard summarising key results in the sector.

Housemark and the Sector Scorecard (UK)

Housemark is a privately operated benchmarking firm in the UK. As a member, a housing provider receives a customised core benchmarking report setting out its results for key metrics against the provider's peer group (determined by whether the provider received its properties through a housing transfer from a council, and the provider's stock size).

In addition to the paid membership service, Housemark also produces the publicly available Sector Scorecard for the National Housing Federation, a trade association for social housing providers in England. The Sector Scorecard sets out first quartile, median and third quartile results:

- Business health (e.g. operating margin, EBITDA MRI%).
- Development (e.g. new supply delivered, new supply %, gearing).
- Outcomes (e.g. customer satisfaction, reinvestment %).
- Asset management (e.g. return on capital employed, occupancy, responsive repairs to planned maintenance).
- Operating efficiencies (e.g. social housing cost per unit, rent collected, overheads as % of adjusted turnover).

In addition, the annual benchmarking reports that members receive include more detailed metrics, with specific comparisons to the provider's own peer group.

Cost allocation guidance

The Sector Scorecard sets out the specific formula for each metric, as well as states that terms should be consistent with the Accounting Direction for private registered providers of social housing. This direction is issued by the UK Regulator of Social Housing, and private registered housing providers must comply with the direction.

The Housemark benchmarking tool requires a detailed breakdown of the housing providers cost centres and employees to be allocated to the Housemark methodology.

Tenant satisfaction surveys

One of Housemark's products is guidance for running consistent tenant satisfaction surveys, within its STAR (Survey of tenants and residents) framework. The development of the methodology followed a UK government decision that ended the requirement to conduct surveys under a previous methodology. The STAR methodology is used by approximately 350 landlords.

The publicly available guidance includes material on choosing a robust sample of tenants, maintaining confidentiality, survey logistics and analysing and responding to results. In addition, Housemark publish a specific set of questions and methodology for undertaking the surveys.

Value for Money metrics (Regulator of Social Housing)

Summary report

Published alongside the Global Accounts (consolidated financial information on the UK social housing sector), the regulator publishes a summary report of its own key value for money metrics. These are largely focused on financial and organisational health, rather than operational performance.

Value for Money – Technical regression

The UK regulator also performs regression analysis to determine the key drivers of the differences in results of key metrics. The key explanatory variables are:

- Supported housing (% of total)
- Housing for older people (% of total)
- Over 50% of their stock via transfers (dummy variable)
- Neighbourhood deprivation ranking
- Regional wage index
- Total size of social stock

Benchmarking International examples (2 of 2)

In Australia, a national perspective on social housing performance and cost is provided through work by the Productivity Commission. At state level, further data is available through industry-led initiatives such as House Keys.

Report on Government Services (Australia)

The ROGS is prepared by the Australian Productivity Commission on the performance of government services. Housing is one of many areas of government spending considered, based on a performance indicator framework of Equity, Efficiency and Effectiveness measures.

The measures in the report include metrics on:

- Priority access to those in greatest need.
- New tenancies allocated to those with special needs.
- Match of dwelling to household size.
- Proportion of tenants rating amenity and location aspects as meeting their needs.
- Dwelling condition meets minimum standards.
- Customer satisfaction.
- Net recurrent cost per dwelling.

The data in the ROGS is generally presented on a state by state basis. The key financial metric is 'net recurrent cost per dwelling'. However, this is generally only comparable over time, rather than across jurisdictions given the different data collection methodologies.

Community Housing Industry "House Keys" (NSW, Australia)

The HouseKeys benchmarking tool is available to community housing providers in New South Wales, and is branded as "by the industry, for the industry". It is based around two separate fields, operational and workforce.

House Key: Operations provides benchmark data on:

- Tenant and housing services (e.g. occupancy, rent arrears)

- Service and asset management (e.g. maintenance costs, asset standards)
- Development (e.g. leverage targets)
- Finance and efficiency (e.g. employee expenses, bad debts)
- Tenant satisfaction (e.g. survey results)
- Demographic information (e.g. tenants with disabilities)

House Key: Workforce provides benchmark data on:

- Workforce (e.g. turnover, qualifications)
- Salaries and expenses
- Board remuneration.

Housing Registrar (Victoria, Australia)

The Housing Registrar publishes annual sector performance and financial information. This includes measures on property turnaround times, rent arrears, occupancy rates, maintenance response times and tenant satisfaction measures.

Benchmarking

Potential approaches to key challenges (1 of 2)

We have considered potential approaches to resolving some of the key challenges set out on previous pages.

This is not intended to be an exhaustive methodology for resolving these issues, but rather to highlight potential approaches that could be investigated further.

Accounting for different management service levels and activities

A key current limitation in benchmarking analysis is a lack of a standard framework and data for systematically capturing differences in tenancy management service levels. The key elements of this could include:

- Disaggregation of 'tenancy and property management' into more granular categories.
- Consistent definitions and terminology, and clear guidance to providers on what costs should be included where.
- Allocation of costs and resources of the provider into the granular components.
- If required, a scoring or grading system to capture the scope of services provided within a category.

Previous work by Hal Pawson has highlighted the limitations of benchmarking in Australia (e.g. unexplainable variance and the unreliability of results published through ROGS). Pawson's conceptual framework is designed to be able to separate out core tenancy management functions (common to all providers) with additional services. The four categories of the framework are:

- **Tenancy management** – core tenancy management, such as inductions, lease management and rent collection.
- **Property and neighbourhood management** – management of properties, such as inspections and managing maintenance requests (but excluding cost of works).
- **Individual tenant support** – tenant support visits, referrals to personal support, managing at risk tenancies.
- **Additional tenant and community services** – supporting tenants to engage with employment or training, community events, management of community volunteers.

Under this framework, providers allocate salary and non-salary costs within these and other non-tenancy and property management categories.

Further approaches

In addition to disaggregating service levels, HUD may wish to consider establishing further:

- **Qualitative service levels:** At a minimum, maintaining up to date qualitative descriptions of the services provided by each CHP to provide contextual information when interpreting benchmarks.
- **Quantitative service scoring:** Designing a framework for quantitatively scoring the level of service within each category. For example, a weighted scoring system between 1-10 on the intensity of employment support a tenant receives. An adjusted cost of provision could be presented taking account of the service level scoring.

Accounting for tenant cohort differences

A frequent comment in the CHP survey was that the CHP's particular tenant cohort required greater resources to support relative to a conventional market tenant (e.g. both for standard tenancy management and in providing additional services). Some potential approaches to account for this could include:

Benchmarking peer groups

This would require collecting information on tenant cohort composition (e.g. proportion of elderly, proportion who report a disability etc), and then benchmarking organisations with similar tenant characteristics.

Statistical analysis

Similar to that used by the UK social housing regulator, this would involve using publicly available (local deprivation indices) and other collected data on tenant cohort composition to support regression analysis across providers.

Benchmarking

Potential approaches to key challenges (2 of 2) and next steps

We consider there is merit in HUD considering the development of a fit for purpose benchmarking approach for Public Housing.

Accounting for housing age and standards

Similar to the approach with tenant cohort, a reasonable understanding of property typology, age and region could enable more 'like for like' comparisons between providers. This would consider broad groupings of 'similar' properties based on age and typology, with analysis done on that basis.

Accounting for regional differences

Many of the previous methods (e.g. regression analysis) could be considered for controlling regional factors. However, they may be of limited value given that many CHPs predominately operate in a single region, and therefore regional weightings derived from the data itself may be difficult. Alternatively, an externally sourced set of broader regional cost weightings could be applied to the data to adjust for regional differences.

Developing guidance on cost allocation

There is no consistent methodology for the reporting of costs in the Public Housing sector. In addition to service categories described earlier, further guidance would support:

- Cost centre allocation into standardised categories.
- Specific cost items to include and exclude within each category.
- The allocation of overhead staff and costs across different management categories, such as office rent, HR costs, and staff training.

Examples of cost allocation guidance for Public Housing is set out in the Appendix of the UK Sector Scorecard and the Accounting Direction for private registered providers of social housing.

Developing guidance on measurement of tenant outcomes

The current inconsistency in the measurement of tenant outcomes limits the comparability between these measures. As discussed earlier, there is scope to publish a consistent methodology for providers to use.

Next steps

We consider there is merit in improving the level and consistency of Public Housing cost and performance information available to inform HUD's purchasing decisions and for the sector to better understand its own costs. There is currently nothing comparable to the benchmarking and reporting in the UK and Australia (even with their limitations).

The key trade-off is the administrative burden and cost that more comprehensive data collection would impose on the CHP sector, as well as the systems required by HUD to capture this information efficiently. Many CHPs are relatively small organisations operating a modest portfolio of properties, and therefore may lack the in-house capacity to engage with data collection exercises. We would suggest that HUD consult with the sector to inform the appropriate balance as it moves ahead with benchmarking.

Lower burden on the sector

- Collection of a qualitative description of services by providers.
- Developing and publishing consistent guidance for undertaking tenant satisfaction surveys.
- Annual reporting of a small number of key performance metrics (this is currently included in HUD's revised contracting framework).
- HUD developing and publishing voluntary guidance on service and cost allocation, and piloting on a small number of larger providers with greater internal capacity.

Higher burden on the sector

- Detailed annual financing reporting for all providers against cost allocation framework.
- Comprehensive reporting on a broad suite of operational performance metrics.

Benchmarking Common and potential Public Housing benchmarks

This table provides a summary of key common benchmarks used internationally in Public Housing.

Metric	Description
Cost of delivery	
Tenancy management cost per unit	Total cost incurred by the provider in the delivery of tenancy management per unit.
Property management cost per unit	Total cost incurred by the provider in the delivery of property management per unit.
Responsive maintenance cost per unit	Total cost incurred by the provider on responsive maintenance per unit.
Planned maintenance cost per unit	Total cost incurred by the provider on planned maintenance per unit.
Major repairs cost per unit	Total cost incurred by the provider on major repairs per unit.
FTE per 100 properties	Number of tenancy and property manager FTEs per 100 properties.
Tenancy management	
Tenant satisfaction with services	Overall level of tenant satisfaction with the provider's services, typically through a tenant survey.
Rent collection and arrears	Measures rent collection from tenants.
Tenancy sustainability	Measures of how long tenants remain in their properties and exit reasons.
Tenant social and economic wellbeing	Measures of broader tenant social and economic wellbeing.
Property management	
Planned repairs expenditure as a proportion of total	The ratio of planned maintenance to total spending.
Turnaround time	The time elapsed between a property becoming available and it being ready to let to a tenant
Tenant satisfaction with their home / repairs and maintenance service	Tenant satisfaction with their home, tenant satisfaction with the repairs and maintenance service
Repairs and maintenance completion and response times	Average completion and response times for different categories of repairs and maintenance requests
Tenant to dwelling matching	The proportion of properties that are matched to the bedroom requirement of tenants. Other metrics can consider location and amenity suitability.
Property standards	The proportion of properties meeting a specified minimum property standard.
Financial sustainability	
Gearing	The proportion of borrowing in relation to total assets (typically Debt/ Debt+Equity)
Operating margin	Operating surplus over total turnover

6

Constraints and risks in current Public Housing funding settings

Constraints and risks in current Public Housing funding settings

Introduction and scope

Based on our work during this review, we identified broadly five potential issues with current funding settings that HUD may wish to consider for further policy work.

Introduction and scope

The scope of this section is to provide a discussion of the constraints, risks and opportunities for efficiencies within current funding settings.

For the purposes of this discussion, we have assumed that the fundamental basis of the system (i.e. providers receive a market rent for each property, composed of a tenant contribution, with an IRRS top-up) remains in place. This is supported by current legislative arrangements where providers are landlords under the Residential Tenancies Act. We have also focused primarily on funding settings, and have not reviewed the contractual terms within HUD's standard agreements with providers.

The material in this section is provided as a discussion, and would require further detailed policy work.

Potential levers within existing funding settings

Given the scope of existing funding settings, the following potential levers are available:

- The method by which market rent is set by providers, which in turn, drives the revenue received by providers and government expenditure.
- The contractual and performance obligations on providers.
- The approach to additional financial payments made available to incentivise and enable new supply.
- The types of information that providers must collect and make available to the purchasing agency.

With those levers in mind, the table on the right sets out five areas for discussion.

Discussion issues

	Issue	Potential constraint, risk or opportunity
A	Funding tools to support new supply	There is now only a single funding mechanism to support new supply, which is not consistent with CHPs' stated preference and cited barriers.
B	Market rent setting approach	The level of market rent drives both government expenditure and provider sustainability, with rent setting for CHPs being subject to older maxima (set in 2016). HNZ is not subject to the same approach.
C	Administration and setting of the OS	The administration of OS for HNZ is in its early stages, and there may be opportunities to review how OS is being set and administered for new developments in the pipeline.
D	Performance regime	There are no financial incentives on providers to improve performance.
E	Data collection and availability	There are significant gaps in data that is readily available to HUD in understanding the cost and performance of the system.

Constraints and risks in current Public Housing funding settings

A. Funding tools to support new supply (1 of 7)

The CHP sector is composed of largely of relatively small organisations with limited balance sheets and development capacity.

We have not focused on HNZ in this section given it does not face similar capital constraints, and therefore more suited to existing new supply support tools.

Introduction

As previously described, the current funding tool to support new supply is the OS, up to 90% of market rent. Previous approaches in the sector have included conditional capital grants, concessionary loans and suspensory loans. This section discusses the advantages and disadvantages to the government considering alternative funding tools for new supply, given the objective to source 30% of new supply through the CHP sector.

Broader issues and assumptions

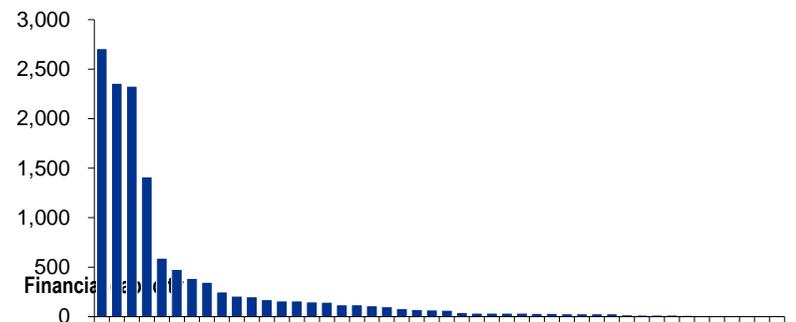
In addition to the specific assessment of different funding tools, we note the following broader issues in the delivery of new Public Housing supply:

- We have assumed that there is a broad preference for providers to build or purchase new properties, rather than enter into lease arrangements for existing properties. This is driven by an interest in increasing overall housing supply, rather than achieve greater Public Housing supply through substitution with general housing stock.
- The government's long term vision for the CHP sector will influence its decisions on the form of funding tools it uses. Ultimately there needs to be a policy decision on whether the government wants to support CHPs to grow their development capability and capacity to undertake property development, or incentivise CHPs to bring on new supply through other means, e.g. direct leasing.
- The government may have a fiscal preference for either operating or capital expenditure and this could drive decisions on the form of funding tool.
- HNZ is in a period of transition as Kāinga Ora – Homes and Communities is established. The nature of the relationship between HUD and Kāinga Ora and the form of funding tools for new supply could change during this transition.

New Zealand CHP sector

The New Zealand CHP market is characterised by mostly smaller providers without significant scale. CHPs are largely social good organisations, many of which are registered charities. Of the 45 CHPs in the HUD supply dataset at December 2018, there were only four CHPs managing more than 1,000 properties, while 26 CHPs managed fewer than 100 properties. In total, the CHP sector manages (through lease or ownership) approximately 13,000 properties, including both IRRS and affordable properties.

Diagram: CHP property portfolio size (December 2018)



The assessment of CHP creditworthiness would include multiple financial and non-financial considerations. Both Moody's and Standard & Poor's publish methodologies for non-profit social housing providers.

While the Charities Commission collects high-level information on registered charities, it is not detailed enough to provide a reliable assessment of the borrowing headroom of the sector. In summary, CHPs in the 2018 charities data had an average leverage of 23% and average gross margin (total income less total expenditure) of 12%. Of the 47 CHPs with sufficient financial data in the dataset, 20 CHPs had a current leverage ratio exceeding 30%. Over half of the CHPs had total assets under \$10m. While further analysis would be required, indicative evidence is that most CHPs have relatively limited financial headroom.

Constraints and risks in current Public Housing funding settings

A. Funding tools to support new supply (2 of 7)

The CHP sector has generally expressed a strong preference for capital support for new supply.

Views of the CHP sector

CHP survey: intentions to bring on new supply

As part of the CHP survey, respondents were asked to describe their medium-term (5-year) intentions for growth of their IRRS portfolios and their approach to achieving this. This was through a free-text box, and we did not specifically ask CHPs to quantify their intentions.

- Almost all CHPs signalled that they are seeking to grow their portfolios over the period, with some indicating a general intention while others provided details of specific upcoming developments.
- The method for bringing on new supply was predominately new build properties on land already owned, gifted land or land that the CHP intends to purchase on the private market. Several CHPs indicated their intention to redevelop and intensify existing properties.

CHP survey: Enablers and barriers to new supply

A follow-up question sought comment from CHPs on enablers and barriers to increasing the number of IRRS places. A summary of key themes is presented below:

- A lack of access to capital funding. The return on existing portfolios are too low to borrow at commercial bank rates, and build costs can be higher than other residential properties given specific design requirements.
- OS does not work for CHPs given it requires significant equity or high levels of leverage that is not a sustainable risk position for a CHP, particularly for a non-profit with modest surpluses.
- The cost and availability of suitable land.
- The tenant groups served by the CHP are not seen as appealing to private landlords who own suitable houses, with tenant groups such as professionals and students being seen as more appealing.

- The levels of 'market rent' being held artificially low by the government, having not been reviewed since 2016, along with high development costs, means that projects are uneconomic.
- A lack of funding given CHPs both provide accommodation but also offers various support services for tenants.

View of CHA

The CHA produced a brief one-pager for HUD in which it described its high-level views on a preference for upfront funding relative to the operating subsidies. Key points from CHA include:

- Capital grants have the benefit of increasing CHP equity, allowing it to leverage off its equity to build its asset base and raise further debt. The experience in the UK is that once housing associations are capitalised, then further subsidy from the government is no longer required.
- Capital grants have lower compliance costs, with assessment only occurring once and ongoing compliance monitored by the regulator.
- OS effectively treats CHPs as agents of the Crown delivering services, rather than recognising the additional value CHPs could bring.

Other public comments

Recent public comments in the media* by Auckland Community Housing providers also indicated their preference for capital support. It was argued that CHPs "are able to make repayments, but unable to find the deposit to get a home in the first place".

* Source: Stuff (1 June 2019)

Constraints and risks in current Public Housing funding settings

A. Funding tools to support new supply (3 of 7)

The assessment of alternative funding tools should consider a wide range of financial and non-financial factors

Key factors for assessing suitability of funding tools	
Factor	Description
Cost to the Crown	The extent to which the funding tool imposes a cost to the Crown, as represented by the NPV of the Crown's contribution over the life of the asset.
Cost of delivery	The extent to which the funding tool supports the efficient delivery of new supply, for example, by reducing the total financing costs of the development.
Alignment with sector preferences/requirements	The extent to which the funding tool aligns with the sector preferences for what the financial barriers are to deliver new supply.
Contracting and implementation complexity	The extent to which the funding tool requires complex contracting/ commercial design to implement which may impose costs on both the provider and the Crown.
Ability to monitor	The extent to which the funding tool supports ongoing monitoring of performance and expenditure, and provides the Crown with transparency and levers to improve provider performance and government decision making.
Risk to the Crown	The extent to which the funding tool may expose the Crown to risks that it is not best placed to manage.
Risk to the provider	The extent to risks are allocated to the provider that it is not best placed to manage.
Capitalisation of the CHP sector	The extent to which the funding tool would support the capitalisation of the CHP sector over the long term (if this is aligned to HUD's sector strategy).
Treatment of residual value at contract end	The treatment of the residual value of the property at the end of the contract term.

Constraints and risks in current Public Housing funding settings

A. Funding tools to support new supply (4 of 7)

We have considered four broad funding options for supporting new supply.

Funding tools	Description	Likely provider/participant preference	New Zealand examples	Key considerations
A. Operating grants	The provider receives an ongoing operating payment for a set period of time (e.g. 25 years) in addition to market rent. The grant amount may be calculated as a cost-based figure or in relation to market rent.	Providers with significant capital base that are able to raise finance for the cost of buying/building the property and then service the debt with the support of the operating grant.	Operating Supplement	<ul style="list-style-type: none"> Stable, predictable cash flows for both HUD and provider. Less capitalised or highly leveraged providers may not be able to bring on new supply (insufficient funds to cover buy/build costs). When calculated relative to market rent this may incentivise new supply in some regions over others. Could attract new forms of finance into the sector. Appeals to financiers that are interested in long-term stable cash-flows.
B. Upfront funding	The government would provide an upfront payment to the provider, which reduces the finance required that the provider needs to raise.	Less capitalised or highly leveraged providers that lack sufficient capital to raise sufficient debt finance.	UF	<ul style="list-style-type: none"> Supports any size providers. Uses government cost of capital. Lower level of private finance. However the cost of risks retained by the Crown need to be considered. Lower risk transfer to private finance and benefit from bank due diligence (if no private debt in the development). Unconditional grant arrangements provide limited protections to the Crown. However, UF includes contractual mechanisms to require repayment if provider does not meet contractual terms.

Constraints and risks in current Public Housing funding settings

A. Funding tools to support new supply (5 of 7)

We have considered four broad funding options for supporting new supply.

Funding tools	Description	Likely provider/participant preference	New Zealand examples	Key considerations
C. Debt arrangements (concessionary loans, “aggregator” products)	The government would provide a loan at a concessionary interest rate (e.g. government cost of funds plus a risk adjusted rate specific to the project), either for a portion or the entire life of the loan. The provider would be required to repay the loan.	Less capitalised providers that cannot raise private finance and/or providers with insufficient operating cash-flow to service a loan at market rates.	HIF	<ul style="list-style-type: none"> • Potentially fiscally neutral (or close to it) over the life of the loan. • Uses government cost of capital. Lower level of private finance. However the cost of risks retained by the Crown need to be considered. • Risk to Crown that loan will not be repaid. Administration of managing loan. • Scope to reclaim funds if provider does not deliver contracted services
D. Crown quasi-equity investment	The government provide upfront funding and holds a quasi-ownership interest (e.g. subordinated debt) in the properties. If the properties are sold within a defined period, then Crown receives a share of gains.	Similar to above B.	SHRP model in Tauranga (Crown Retained Investment)	<ul style="list-style-type: none"> • Similar to arrangements in B, but may include some equity-like features (i.e. Crown sharing in portion of capital gain if property sold within period). • Protects Crown investment in Public Housing. Lower risk of value leakage to provider. • Potentially greater administration to manage the arrangement.

* In 2017, the Australian government established the Affordable Housing Bond Aggregator (AHBA). The AHBA sources capital from the bond market to provide lower interest long-term loans for non-for-profit CHPs to develop housing. This is intended to reduce financing costs for CHPs relative to what they could access themselves from a bank. The AHBA acts as a loan guarantor.

Constraints and risks in current Public Housing funding settings

A. Funding tools to support new supply (6 of 7)

The table summarises the key considerations for the funding tools, based on the criteria set out earlier.

It is likely that a mixture of tools will be useful in New Zealand due to the variety of:

- Providers (i.e. different scales, capital structures and operating models)
- Property markets (e.g. different rent levels, land prices, cost to develop)

	A. Operating grants	B. Upfront funding	C. Debt arrangements	D. Quasi-equity
Cost to the Crown	Marginally higher under an operating grant to provide similar level of subsidy		Lower than grants assuming some repayment obligation	Similar to B.
Cost of delivery	Marginally higher under an operating grant assuming government's cost of capital is below private		Similar to B	Similar to B
Alignment with sector preferences/requirements	Lower	Higher	Medium	Medium
Contracting and implementation complexity/ongoing burden	Lower	Lower	Higher	Higher
Ability to monitor	Higher	Medium	Medium	Medium
Risk to the Crown	Lower – Crown does not pay until construction complete. Benefit of private lender due diligence	Medium – Crown manages risk through contracted milestone payments and upfront due diligence	Medium – Upfront due diligence required	Similar to C.
Capitalisation of the CHP sector	Only in later periods of the contract with higher free cash flow	Immediate capital injection	Subject to policy design	Similar to B (but subject to policy design)
Treatment of residual value after contract end	Retained by provider	Retained by provider	Retained by provider	Retained by provider (unless sold within defined period)

Constraints and risks in current Public Housing funding settings

A. Funding tools to support new supply (7 of 7)

We consider there is merit in increasing the range of funding tools to support new supply delivery by CHPs.

Comments

- There are **no objectively superior** options for providing support for new supply in the CHP sector
- The choice **between capital and operating mechanisms is not primarily a choice about cost to government**. While there is likely to be a marginal saving from approaches that provide capital to CHPs (from a lower cost of government funds), the risk-adjusted cost of capital for the Crown is not likely to be a major determinant of a preferred funding mechanism.
- Given the above and the aspiration for CHPs to bring on 30% of new supply, there is merit in HUD considering **a wider range of funding tools** to support new supply that are **likely more closely aligned to the requirements of the CHP sector**.
- In all cases, HUD **needs to be comfortable with transferring value to external, regulated organisations**. At the end of a contract or encumbrance period, a CHP could realise the full market value of the property for which a significant Crown contribution has been made. In exchange, the Crown is receiving 25 years of service that would likely not have been provided without the subsidy.
- Particularly for projects that do not have a privately financed component, **the government should continue to undertake robust due diligence over proposal regardless of the funding mechanism used**.

Constraints and risks in current Public Housing funding settings

B. Setting of market rent (1 of 3)

We consider there is benefit in further work on market rent setting in the sector to improve transparency for HUD as the purchasing agency and achieve a more level playing field across providers.

Introduction

The level of market rent is both the key driver of provider revenue and government expenditure through the IRRS. As set out in section 2, HNZ updates market rents quarterly under a two stage process, based on its own benchmarking process. CHPs determine market rent in accordance with their own policies, but must set rent levels within region and typology rent maxima set by HUD. The rent maxima were last updated in 2016.

The current arrangements raise the following potential issues:

- There is a difference in rent setting approach for different providers in the sector.
- HUD as the purchasing agency doesn't necessarily have clear visibility or control over its key cost driver.
- The rent maxima haven't been updated since 2016, creating the risk of significant divergence from market values. HUD does not currently have a market rent setting policy.

CHP rents relative to current maxima

Based on data provided by HUD as at April 2019, we observe that:

- Around 8% of properties were above the rent maxima, with 95% of these properties being within \$100 of the maxima.
- Of the 92% of properties below the maxima, 53% are under the maxima by less than \$100, while 43% are between \$100-\$200 below the maxima.
- On a regional basis, Hamilton City, Napier City and Wellington City had between 40-63% of properties above the maxima, the highest proportions for areas with greater than 30 properties.

We understand from HUD that properties can be over the limit for a number of reasons, including the management top-up component for redirect properties above market rent and properties where rental indexation is contracted (i.e. capacity contracts).

Table: Top 10 CHP areas (by total number of properties)

	% over	\$101+ under	\$1-100 under	\$0-99 over	\$100+ over	Total
Auckland - Central	7%	1795	844	183	2	2824
Tauranga City	5%	13	1016	49	3	1081
Christchurch City	2%	384	395	16	0	795
Auckland - South	5%	308	176	21	5	510
Auckland - West	6%	125	145	15	1	286
Hamilton City	54%	3	54	62	5	124
Auckland - North	1%	27	73	1	0	101
Western BOP	1%	0	97	1	0	98
Wellington City	40%	11	42	27	9	89
Masterton District	8%	5	52	5	0	62
Napier City	63%	0	15	25	0	40

HNZ rents relative to current maxima

Based on the same dataset as above, we observe that:

- Approximately 12% of HNZ properties are above the rent maxima, with 97% of these properties being within \$100 of the maxima.
- Of the 88% of properties below the maxima, around 51% are under the maxima by less than \$100, while 42% are between \$100-\$200 below the maxima.
- A regional view of HNZ properties above the market rental maxima is provided on the following page. As shown, the overall average hides significant regional variation where a larger proportion of properties in a region are over the maxima.

Constraints and risks in current Public Housing funding settings

B. Setting of market rent (2 of 3)

While only a small proportion of HNZ's properties are above the rental maxima, this hides significant regional variation.

Table: Highest proportion of HNZ properties above maxima (with >30 properties in total within the region)

	% over	\$101+ under	\$1-100 under	\$0-99 over	\$100+ over	Total
Waipa District	96%	0	9	203	3	215
Tauranga City	83%	1	31	152	6	190
Whakatane District	81%	54	40	395	8	497
Rotorua District	67%	2	209	417	8	636
Upper Hutt City	66%	0	129	254	1	384
Matamata-Piako District	62%	1	63	106	0	170
Hauraki District	55%	0	49	59	0	108
Lower Hutt City	45%	3	1772	1446	13	3234
Marlborough District	45%	0	230	188	1	419
Hamilton City	34%	13	1896	968	5	2882
Thames-Coromandel District	32%	0	142	66	0	208
Wellington City	31%	109	1147	479	81	1816
Gisborne District	28%	114	775	351	1	1241
Nelson City	24%	7	422	134	0	563
Waimakariri District	23%	2	106	32	1	141
Porirua City	22%	17	2004	575	10	2606
Kapiti Coast District	20%	0	167	43	0	210
Tasman District	17%	6	123	26	0	155
Kaipara District	13%	0	99	15	0	114

Sufficiency of current rental maxima

The current rental maxima appear to be out of step with market rents in a number of regions around New Zealand. This is evidenced on two fronts:

- The proportion of properties above the maxima is particularly high in specific regions, even though the total number of properties in the entire Public Housing portfolio over the maxima is relatively modest.
- As shown below, the mean and lower quartile market rents in areas with a relatively high proportion of properties above the PHP limits are now close to or exceeding the maxima levels.

Table: Mean and LQ market rents for houses and flats/apartments relative to PHP limits (2 bedroom properties)

	Lower Quartile	Mean	PHP limit
Waipa District	\$339	\$384	\$300
Tauranga City	\$384	\$430	\$350
Whakatane District	\$298	\$340	\$300
Rotorua District	\$295	\$341	\$300
Upper Hutt City	\$340	\$369	\$350
Matamata-Piako District	\$280	\$302	\$300
Hauraki District	\$255	\$300	\$300
Lower Hutt City	\$389	\$509	\$350
Marlborough District	\$298	\$332	\$300
Hamilton City	\$340	\$370	\$350
Thames-Coromandel District	\$334	\$351	\$300
Wellington City	\$452	\$517	\$450
Gisborne District	\$256	\$295	\$300

Source: Market rent and Lower Quartile rent are based on June 2019 MBIE rental data

Constraints and risks in current Public Housing funding settings

B. Setting of market rent (3 of 3)

On balance, there appear to be sound policy reasons for retaining rental maxima for Public Housing.

However, there is not an obvious rationale for the current uneven playing field between providers that we are aware of.

Level playing field

Under current arrangements, HNZ is not subject to the same rental maxima as the CHP sector. We are not aware of the policy rationale for this differential. In the interests of promoting a level playing field between providers performing similar services, we consider there is benefit in HUD considering whether the maxima should apply across the entire Public Housing sector.

Transparency of market rent setting

HNZ currently undertakes its rent setting through a quarterly market benchmarking approach, supported by an audit process. While we have not considered this process in detail, we see benefit in:

- Ensuring that HUD as the purchasing agency has transparency and input into provider rent setting methodologies.
- A more consistent approach to rent setting across providers and/or information sharing on rental benchmarks.

Given the apparent divergence from market rents in some regions, there is a case to consider updating the maxima. While this is somewhat mitigated by the flexibility of the OS available for new supply, a sustained period of divergence from market rent may lead to:

- Underinvestment or exiting of properties in particular regions.
- Unequal treatment between HNZ and CHPs providing a similar service at different price levels.
- HUD potentially receiving fewer proposals from CHPs who may assume that HUD does not have flexibility with regard to market rents.

Rental maxima as an ongoing policy tool

The following table provides a discussion of factors in considering the utility of rental maxima as a policy tool.

Factor	Comment
Reflects market conditions	There is an inherent risk that maxima become out of step with market conditions (leading to underinvestment in that region). However, this can be mitigated through systematic and regular updates and/or permitting a certain percentage of properties within a portfolio to exceed the maxima.
Administrative burden	Arguably reduces some of the administrative burden by lowering the monitoring required of rent setting policies by providers (assuming compliance with the cap can be easily established). No significant impact on provider administrative burden.
Fiscal control	As a starting principle, we consider it preferable that the purchasing agency has some control levers over the price it is willing to pay a supplier in a given location. The rental maxima also provides greater certainty of future Public Housing spending.
Sector signalling	Rental maxima provide a signal to providers of the type of property that the government is willing to pay to be a Public Housing place. While the rent maxima should be sufficient to provide for warm and dry houses, properties with rent values significantly higher than the mean come at high cost to government and create inequities with other renters (i.e. the level of subsidy for an occupant is far higher than an individual in similar circumstances in another Public house or market rental).

Constraints and risks in current Public Housing funding settings

C. Administration and setting of OS (1 of 2)

The current approach of considering whole of life project costs and revenues for CHP developments is sound, alongside an assessment of the project deliverability of the CHP.

We would however support more transparency on how OS is determined across different development proposals (e.g. targeting a specific equity IRR, cash-flow neutral over a defined period).

Introduction

The OS is now the primary funding tool to support Public Housing new supply. The administration and setting of OS drives both government expenditure and the incentives on providers to bring forward new supply proposals.

CHP OS setting

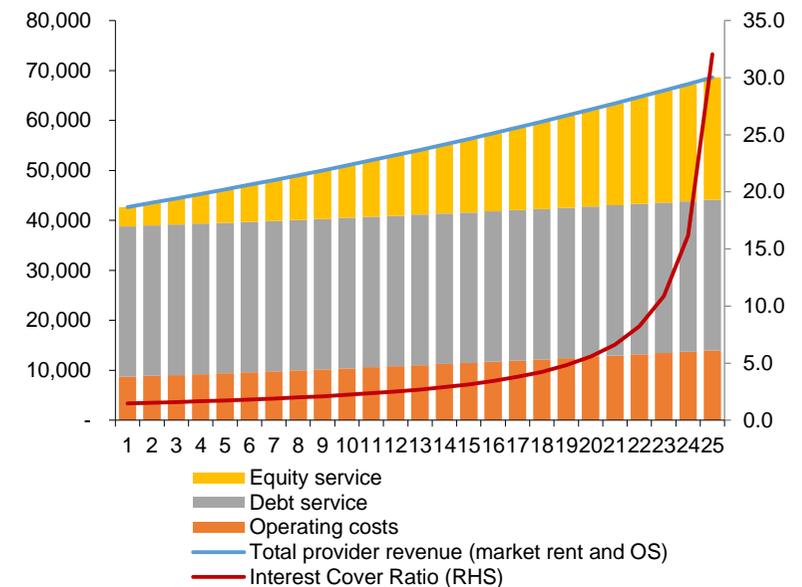
OS is assessed for CHPs through a formal two stage procurement process managed by HUD.

Cash-flow profile over the life of the project

As shown on the right, a typical development project with OS is expected to generate increasing cash-flows to equity (i.e. free cash-flow after payment of operational costs and debt servicing). This represents the CHP (or its equity investor's) return on its capital invested in the project.

- On the assumption the project includes an equity contribution, the increasing free cash-flows to the CHP in later project years is not necessarily a value for money concern. These cash-flows support the CHP investor to achieve a target rate of return, as represented by the equity IRR. The small cash-flows in the early years of the project alone would not alone generally be sufficient to meet this target.
- Where a CHP requires a higher level of OS% to ensure a sufficient ICR in early project years (but would result in a return greater than comparable projects), there is merit in HUD having flexibility for the OS% to be lowered after a specified number of years in the project to avoid instances of excess returns.
- In the case of a project without an equity contribution (e.g. debt financed and government payment), the surplus cash-flows would effectively represent a further grant to the CHP (i.e. the CHP is receiving a return without 'skin in the game'). This may be desirable from a policy perspective to support the capitalisation of the sector, but needs to be considered alongside arrangements in other potential CHP developments that HUD could choose to support.

Diagram: Uses of cash over life of a development



Reporting and cost monitoring

Given the OS% is based on business case figures, there is a potential risk that actual costs differ (higher or lower) than those on which the OS was calculated. In a typical project finance arrangement, this risk would be borne by the party undertaking the project, with the Crown achieving comfort through the procurement process that total whole of life costs represent value for money.

Gains from refinancing are usually shared between the Crown and the project, and the costs of some services may be recalculated on a periodic basis. While a typical PPP approach is likely to be too administratively burdensome given the large number of projects, there is merit in CHPs reporting actual (construction and operating) costs to support HUD's ongoing benchmarking.

Constraints and risks in current Public Housing funding settings

C. Administration and setting of OS (2 of 2)

We have not undertaken a detailed analysis of HNZ's investment decision making process.

While not necessarily unreasonable, the IROI metric is a very basic approach to the calculation of OS that differs from that used for the CHP sector.

HNZ OS setting

HUD is currently finalising its agreement with HNZ on the reporting and payment of the OS. HNZ and HUD have agreed that, on a new supply portfolio level, the combined OS will not exceed 50% of market rent. The actual level of OS that HNZ receives per property will therefore differ from the OS that HNZ may have calculated or would otherwise claim for a property.

HNZ's calculation of the level of OS required for a new supply property is primarily based on its *Incremental Return on Investment (IROI)* financial metric. The definition is set out in its Financial Manual as:

$$\frac{\text{Incremental Earnings}}{\text{The total cost of capital investment (excluding existing land)}}$$

Incremental earnings formula

	Existing	Investment
Market rent	Actual	Estimate
Less: Vacancy	Estimate (default: 2%)	0.5%
Less: Maintenance (opex)	Estimate	Estimate
Less: Rates	Actual	Estimate
Less: Management overhead	\$3,040	\$3,040
Less: Tax	28%	28%
Less: Capital replacement	Estimate	Estimate
= Net cash-flow	Sum of above	Sum of above
= Incremental earnings	Investment – Existing net cash-flow	

The maintenance and capital replacement assumptions are based on the typology and age of the asset, based on a 50 year life of the asset.

Total cost of capital investment

The total cost of capital investment is the present value of the cash outlay for the investment, less capital costs foregone (i.e. deferred maintenance to bring the property to condition to maintain the current rental)

IROI hurdle rate and calculation of OS

The IROI hurdle rate is the minimum IROI that an HNZ investment must meet to meet its cost of capital. This is calculated on the basis of HNZ's Weighted Average Cost of Capital (WACC) less an assumed 3% capital growth factor. In other words, rental yield from the investment must exceed 2.89%

The calculation of OS is based on the level of additional market rent from the new development required for HNZ to meet its IROI hurdle rate (or 90% of the rental cap in the region, whichever is lower).

Comment

- IROI is a very simple metric based on year 1 costs only. While it can produce similar results to a highly simplified whole of life model, a more detailed whole of life approach (such that now adopted for CHPs) would be more standard for investment decision making.
- A further key difference is that HNZ's approach calculates a proposed OS% mechanistically to meet its cost of capital. This reflects that the CHP sector does not have a single cost of capital, but is a notable difference between the approaches.
- The calculation of OS for HNZ redevelopments can include consideration of lost rent income from existing properties which increases the level of OS calculated per additional unit. It is arguable whether this should be the case, and HUD may wish to consider it further in the future.
- HNZ's WACC is based on a 2016 calculation and therefore could be updated. Further, HNZ's current cost of equity is arguable given the government's current dividend expectations.
- It is important that as HUD, as the purchasing agency, should have clear visibility of all factors that impact the calculation of OS for a particular development. We support open and transparent data sharing between HUD and HNZ regarding the calculation of OS.

Public Housing policy settings

D. Data and reporting improvements and E. Performance incentives

We consider that improving the scope and quality of data on the CHP sector should be HUD's priority to better understand and monitor performance in the system.

However, over time, as the sector matures and data improves, we consider there is merit in exploring a financial performance regime, similar to that proposed in the Christchurch SHRP transfer.

D. Data and reporting improvements

We have described in section 3 and section 5 the current limitations in data on the performance of Public Housing, particularly the CHP sector. This is a key constraint that HUD faces as the purchasing agency. In considering data improvements, it is important to recognise that measurement is not costless nor explicitly paid for through market rent. The benefit of additional reporting and data collection needs to be considered against this cost to both HUD and the sector.

As discussed in those sections, we consider that HUD should explore:

- consistent reporting formats and definitions of key operational performance metrics, with clear methodological guidance.
- a consistent methodology for the measurement of tenant satisfaction across the sector.
- a consistent method for cost allocation.

Further, HUD should maintain a robust relationship with HNZ, including reporting on key financial and performance metrics, building on current practice. The establishment of Kāinga Ora – Homes and Communities provides an opportunity for HUD to continue to build this relationship.

E. Financial performance regime

We consider the short-medium term priority should be improving data collection and reporting within the sector. Over time, this may indicate that existing contractual mechanisms are sufficient to achieve the desired levels of performance. However, there may also be scope to consider whether financial incentive mechanisms could improve system performance (as have been used in recent New Zealand procurement of infrastructure projects).

This could potentially come in two forms, which could be used either together or separately.

- A performance **abatement** regime to incentivise the provider to meet minimum performance. This has previously been used in numerous New Zealand PPP projects, including schools and prison projects, and outsourced service contracts.
- A performance **outcomes reward** to incentivise providers to achieve performance 'over and above' a baseline level of performance. This could harness a provider's close relationship with tenants to improve tenant outcomes. This style of incentive regime is currently used in the Wiri Prison PPP where a reward is provided for better-than-benchmark recidivism.

Abatement regime

A typical design of abatement regimes is based on the accrual of 'service failure points' when the Provider does not meet specified performance standards. The total accrued points (although sometimes with a write-off of a small number of points in a period) are multiplied by a per-point deduction amount to equal a total deduction. The minimum performance standards could include requirements to meet a minimum standards regarding tenant satisfaction, repairs and maintenance responsiveness and timely tenant induction.

The calibration of an abatement regime needs to achieve a balance between giving providers sufficient incentive to meet the standards, while not causing financial instability for the Provider. In the case of small CHPs, there is likely to be only limited capacity to withstand significant deductions and therefore any approach would need to be carefully implemented.

7

Potential areas for funding setting reform

Public Housing policy settings

Introduction

The government has used a market rent approach to funding public housing for many years. It is worthwhile considering whether this approach best meets the principles of an efficient and effective system.

Introduction

We have been asked to identify areas for potential reform in funding settings for Public Housing. As detailed earlier in this report, the current funding model is a shared contribution from the tenant (IRR) and government (IRRS).

The nature and scale of the IRR is a social policy decision and is outside the scope of this project. We have also not considered alignment with other housing support programmes (e.g. AS). The focus of this section therefore is on how the total revenue for a provider is set and the nature of the HUD payment.

Dimensions of funding settings

When considering a funding approach it is important to consider:

- The total level of funding over the long term and how this is calculated.
- The incentives the approach creates for different parties in the system.
- The levers available to different parties in the system.
- How the risks are allocated to different parties (e.g. if costs are higher than forecast then which party is responsible for securing revenue/funding).
- Transparency and the nature of the information flows that different parties receive.
- Flexibility to adapt over time to different market conditions, different regions and different types/scale of provider.
- Administrative simplicity.

Principles for efficient and effective funding settings

Based on the above, we have developed some high-level principles to guide development of a funding approach:

- A. Funding is provided at a sustainable level that enables the desired outcomes to be delivered and physical assets to be managed responsibly over their life.

- B. The funding approach incentivises efficient delivery of the services.
- C. The funding approach supports growth and further investment.
- D. The funding approach supports consistent levels of service and subsidy across different cohorts.
- E. The funding approach provides flexibility and predictability to government in its purchasing decisions (i.e. can adjust purchase of outputs/outcomes)
- F. The funding approach provides sufficient flexibility for providers to conduct their day-to-day operations and respond to the needs of current tenants.
- G. There is sufficient transparency on the costs of delivery by different parts of the system to allow informed decisions on the allocation of resources over both a short term and long term horizon. Further, there is sufficient transparency on the relative performance of different parts of the system to allow performance improvement over time (individual provider and system) and risks to be flagged in a timely manner.

Context for the current funding approach

Public housing providers in New Zealand are typically arms length bodies that make relatively independent decisions on:

- Day-to-day operations, including corporate management and the level/nature of tenancy management services
- Maintenance and renewal of their existing portfolio
- Investments in new properties and disposal of existing properties.

The system and supporting legislative framework is fundamentally based on the payment of rent to HNZ and CHPs as managers of properties, similar to a regular landlord. This paradigm is the basis for the overall structure of current funding settings.

Public Housing policy settings

Constraints of existing paradigm

The current funding system has a number of constraints, and there has already been a shift away from a pure market rent based model for new supply projects.

Challenges in the existing funding paradigm

- Public Housing generally is held for a long period of time, often with an intention to hold for the entire life of the asset. There is therefore no opportunity to realise capital gains made over time, which represents a major difference from non-Public Housing landlords. Particularly in an environment where investors anticipate a larger proportion of their total return to be derived from capital gain, this results in a lower rental yield that produces challenging economics for new supply projects.
- The level of government expenditure is driven by broader market forces related to the supply and demand of housing in particular regions, rather than deliberate policy decisions to adjust purchase prices.
- Public housing tenants often have higher needs than tenants in the private rental market and therefore tenancy management costs are generally higher. While there is a general expectation that providers provide additional services to tenants, these are not explicitly funded for and there is no current lever for the government to adjust payment for these services (i.e. based on tenant cohort and needs).
- The cost of capital for a Public Housing provider may be different than that of a private landlord, and isn't necessarily straightforward to consider:
 - A provider may be supported by grant funding or similar (e.g. discounted access to land, impact investment at sub-commercial returns) and so does not face the traditional cost of capital itself. However, these providers still face choices in how funds are best deployed.
 - A large portion of the existing HNZ's portfolio is relatively old without associated debt, so generates significant free cash-flow. While HNZ does not currently have dividend expectations, it does require this free-cash to fund a significant asset renewal programme.

Consideration of current funding settings

Principle	Rating	Comment
Funding is at a sustainable level	Green	Provides sufficient funding to cover operational costs of existing portfolio, although providers accept lower total return on their invested capital than other landlords.
Incentivises efficient delivery	Yellow	Cost escalation (relative to market average) risk sits with the provider.
Incentivises new supply	Red	Market rent without further subsidy (such as the current OS) is unlikely to encourage new supply given current development economics.
Consistency and equity	Yellow	Funding allocated for tenancy support services likely to differ by region and provider. Some tenants receive significantly higher subsidies than others.
Flexibility and predictability	Red	Few levers for government to adjust its investment in different areas of the cost stack.
Flexibility for providers	Green	Providers are free to allocate their total rental income as they see fit in managing their portfolio.
Transparency in costs and performance of delivery	Yellow	Currently low for some parts of the sector given current data gaps. This could be addressed through reporting and data collection within the existing funding system.

Public Housing policy settings

Potential other approaches

There are a number of alternative models that HUD could consider for rent setting in Public Housing.

We have not sought to provide an exhaustive option set or evaluation of these as part of this review, but do highlight common models used internationally.

Alternative approaches to rent setting

Approach	Description
Tenant rent contribution	
Proportion of income	Current system where IRR is based on a maximum 25% of the tenant's income
Residual income	Similar to the above, but based on residual income after approximated expenditure is removed (can vary based on household types and characteristics)
Fixed amount	Tenants of similar cohort and area pay a similar rent amount (although can be adjusted based on property specific characteristics)
Proportion of market rent	Similar to some current affordable and council housing, tenants pay a proportion (say 80%) of market rent for the property
Total income received by provider	
Market rent	The existing funding model where providers receive an estimate of the actual market rent for a property
Proportion of market rent	As above, but providers receive a proportion of the actual market rent
Formula rent	The rent is set in accordance with a formula (see UK example).
Cost-based	The rent for a property is based on the estimated cost of delivery.
Other approaches not linked to cost	Other approaches that do not link provider income with cost to deliver in some form (i.e. based purely on tenant income)

Example: Formula rent approach in the UK

The rent setting policy is set by the UK social housing regulator, which seeks to balance the protection of tenants, taxpayers and supporting the delivery of new houses and management of existing properties. The majority of properties are rented under a 'social rent' arrangement, which is set by a formula, based on:

- 30% of the rent is based on relative property values
- 70% of is based on relative local (county level) earnings
- a bedroom factor is also applied

The calculation remains based on 1999 property values, but the calculated rent is inflated by the Retail Price Index (2001-2015), and then the Consumer Price Index + 1% point each year. Housing providers have the flexibility to set rents up to 5% above the formula rent. The housing provider must also sit under the Rent Cap.

Tenants are supported to pay their rent through a Universal Credit transfer (which replaces the previous Housing Benefit).

Cost-based approach

For the purpose of this report, we have considered the cost-based approach in more detail on the following two slides.

Public Housing policy settings

Cost-based approach (1 of 2)

A cost-based approach would be based on setting rents to match provider costs of Public Housing.

Public Housing cost stack

The cost stack for a Public Housing provider is broadly as set out below. Under a cost-based approach, rent would be set in accordance with meeting these costs, similar to a cost stack used for regulated utilities.



Comment

A cost-based approach would involve the calculation of the cost stack for a property based on its characteristics (e.g. age, value, location etc). A potential advantage of this approach is that it allows the explicit funding of each component, with flexibility by government to fund (and measure delivery of) particular outcomes.

Tenancy management

Under a cost-based approach, there is opportunity to adjust the level of tenancy management funding based on tenant characteristics. This differs to the existing model where funding is based purely on property characteristics. Features of this could include transparent funding for:

- Base funding for core tenancy management, adjusted for:
 - Variable service levels above core tenancy management (e.g. meals provision)
 - Tenant cohort characteristics (i.e. weightings based on risk factors)

A broader policy question is whether the government wishes for Public Housing providers to provide a wider range of social services. While the close relationship with the tenant can mean the provider is well-positioned to understand tenant needs, an alternative approach would be to direct additional funding to established social services.

Return on capital

If Public Housing were to be considered similar to a regulated utility, the return on capital could be calculated on the basis of the net rental yield the properties would generate in the market. There are a number of issues to work through as part of further policy work:

- The impact of a lack of a dividend expectation for HNZ. As set out in the LTIP, free cash-flow is used to support new supply.
- For existing properties, CHPs may have benefited from grants or philanthropic funds.

Public Housing policy settings

Cost-based approach (2 of 2)

The advantage of a cost-based approach is increased transparency and financial sustainability, but it would place greater responsibility on HUD to set funding at the right level.

Table: High-level advantages and disadvantages

Potential advantages of a cost-rent approach
More ability to align funding with the true cost to own and operate
Greater transparency over the expenditure and outputs in the system
HUD can have a more active role in specifying service level expectations
Removes need to cross-subsidise
Potential disadvantages of a cost-rent approach
Requires reliable data to set the level of funding
Level of funding may become out of date if there are system changes and need to be reviewed regularly
Likely to require auditing from HUD to get comfort level of funding is correct
Risk of cost increase may sit with HUD

Comment

We have not undertaken an in depth review of alternative models as part of this review. Any fundamental shift in the funding paradigm requires further policy work and research by HUD. However, we do see merit in considering whether a shift to an alternative rent model would improve transparency and financial predictability for the Crown.

8

Housing First

Housing First Introduction

Housing First is focused on supporting the long-term homeless or those who are homeless with complex needs.

Background to Housing First

Housing First (HF) is a relatively new housing support programme, first funded in 2017, that is targeted at supporting people who have been homeless for a long time or who are homeless and face multiple and complex issues. These may include addiction, mental and physical health issues, or experience of violence and abuse.

The programme is based on five principles:

- Access to housing with no readiness conditions.
- People have choices and self-determination about the housing and support they receive.
- Individualised person driven support offered for as long as the person needs.
- Recovery focus with holistic support to reduce harmful behaviour.
- Community, whānau, hapū and iwi connections/integration.

The HF model is based on similar models used in Canada, the United States and United Kingdom. Its origins are based on work completed in New York in the 1990s to support homeless people with a place to live, without requiring them to pass tests or attend programmes as a condition to access housing.

HF was first funded in New Zealand in 2017, and delivered by a collective of providers in Auckland. It subsequently expanded to Christchurch and Tauranga in 2018, and is expanding across the country in 2019, including Hamilton, Rotorua, Wellington, Whangarei, Mid-Far North, Nelson, Blenheim and the Hawke's Bay.

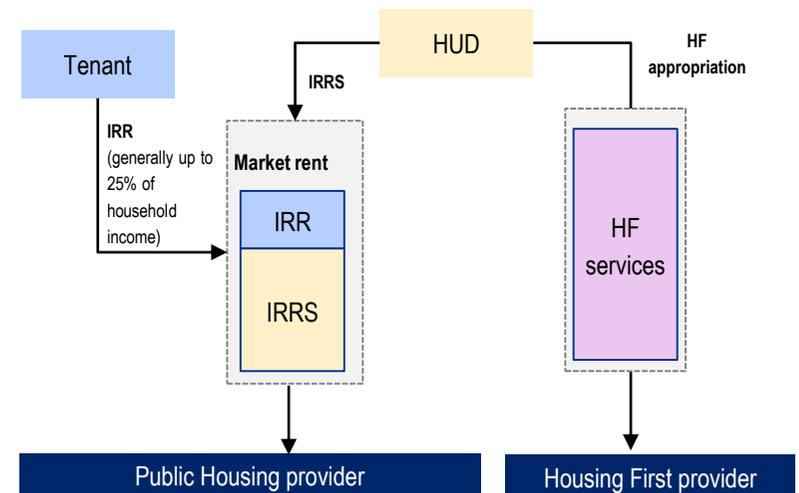
HF funding model

The individuals and whānau supported by HF are able to choose the type of housing that they live in, and where possible, where they live. In practice, HF tenants are predominately in Public Housing provided by CHPs, with a smaller number in private rentals or HNZ Public Housing.

The accommodation cost to government for the majority of HF tenants is therefore paid through IRRS funding streams, similar to any other Public Housing tenant. There is also some costs to government for the Accommodation Supplement for those tenants in market rentals. HF clients enter into a tenancy agreement with the housing provider and must meet their relevant rental obligations.

The service component of HF is funded through a separate stream to HF providers. This is intended to cover the Provider's costs in the engagement of HF clients, housing those clients and then providing wrap-around support services.

Diagram: High-level HF funding flows (where tenant is in Public Housing)



Housing First Contract arrangements

HUD contracts with HF providers are typically for a period of two years, during which the provider is funded to achieve a pre-defined number of outcomes. An outcome is defined as the recruitment, housing placement and ongoing support of an individual or whānau in the HF target cohort.

HF contracting arrangements - overview

HF providers typically enter into a services agreement with HUD for a period of two years. The contracted payment amount is derived with reference to the number of anticipated outcomes, rather than the number of actual outcomes within the period. For the purposes of this analysis, an HF 'outcome' is defined as one individual or whānau being recruited into the programme and successfully housed.

The key contractual arrangements include:

- Provider will have regular support meetings with clients, at a minimum of once per week.
- Assessing the needs of HF clients and ascertaining any risks.
- Provide support to clients, for example, to reduce the harm from substance use, minimising the risk of self-harm and promoting recovery in mental and physical wellbeing.

HF contracting arrangements – maintenance clients*

The two-year contracts between HUD and the HF providers are designed to fund the services provided in order to engage, house and support HF clients phased over the period.

To date, HUD has only re-contracted with providers in Auckland, which receive funding for "maintenance clients" based on their assessment of the required level of ongoing wrap-around services for HF clients engaged/housed in earlier contract periods. The levels include high, medium and low intensity and receive respective quarterly funding per client.

HF contracting arrangements - reporting

HF providers must comply with monthly reporting requirements. These include:

- Client information, including their existing living situation.
- The housing status (currently housed, previously housed, not housed) and the date when a client was housed (if applicable).
- Type of housing (e.g. private, IRRS through CHP/HNZ).
- Number of interactions in the last month.
- Service outcomes (continued need for support, transferred, withdrawn).

In addition to the above, providers are also required to provide quarterly, qualitative information on what, in the provider's view, is working or not effective, types of services that clients are receiving and success stories. We were not provided with this information and have not sought to analyse it for the purpose of this report.

Re-contracted providers are also required to report on the intensity of services provided to maintenance clients.

Housing First

Scope of data

Our cost analysis is primarily based on the pro-forma cost templates submitted to HUD by providers as part of the contracting process.

While the templates drive the contracting costs incurred by HUD, they may not necessarily reflect the actual delivery costs of providers.

HF cost templates

As part of the procurement and contracting for HF, HF providers must complete a cost template setting out the level of resources they require over the contract period. This is based on:

- A phasing of a number of outcomes every six months over the two year contract period (to account for an expected ramp-up in clients).
- Annual operating cost estimates, such as office rent, vehicle lease costs, utilities and cleaning.
- Staffing costs, such as specialist support staff, outreach, case working and additional tenancy management.
- General overhead costs.
- Property costs, including setting up client houses, meth testing, maintenance and other (vacancy, utilities) not covered by the landlord.

Scope of cost data

Our cost to deliver analysis is based on analysing the completed pro-forma cost templates from five HF providers, which HUD considered representative for the purpose of this analysis.

- Four of these have been contracted (and thus, have submitted pro-forma templates) for the first time. One provider was re-contracted.
- One represents a collective pro-forma template submitted by five different entities. Two entities in Rotorua have submitted separate pro-forma templates, which we have combined given the sub-contracting relationship between them.
- The other three completed pro-forma cost templates are from one provider in Christchurch and two providers in Wellington.
- Each pro-forma cost template reflects a different two year period.

Scope of performance data

Our performance analysis is based on the performance reporting data submitted by HF providers discussed on the previous page.

We have been provided with an anonymised overview of all HF clients and their statuses at 31 March 2019. However, we were informed that some of the information could not be relied upon for this report as the process of data collection and reporting across providers has been inconsistent. HUD has informed us that they have taken steps to improve reporting data in the future.

Housing First Cost to deliver analysis

The data in the cost pro-forma indicates the average cost per outcome ranges between NZ\$28k and NZ\$38k between providers over a two year contract period.

These costs do not include accommodation costs associated with the tenants as these are generally funded separately through IRRS or AS.

HF cost templates: Average cost per outcome

The pro-forma cost templates show the providers' annual operating cost estimates as well as the contracted number of outcomes over a two year contract period. An outcome represents a HF client being engaged in the programme, housed and then supported during the contract period. Due to varying assumptions regarding the phasing of outcomes and the phasing of costs, we have sought to analyse the average cost per outcome over both years.

Across all five providers, the average cost per outcome ranges between NZ\$28k in Auckland and NZ\$38k in Christchurch. Further, we have considered the cost benchmark data that the HUD HF team developed to assist in their contract negotiations.

We note that the provider collective in Auckland was the first HF provider and the analysed pro-forma cost template reflects their re-contracting cost estimation. The lower cost per outcome for these providers may be evidence of scale benefits (although this is not observed across the other providers), or may be evidence of a refined model based on their experience during the first contract term.

HF maintenance clients

For HF maintenance clients, providers receive additional payments on a quarterly basis:

- \$6,914 (excl. GST) for high intensity clients
- \$4,341 (excl. GST) for medium intensity clients
- \$3,250 (excl. GST) for low intensity clients.

Diagram: Average cost per outcome and provider (over both years)

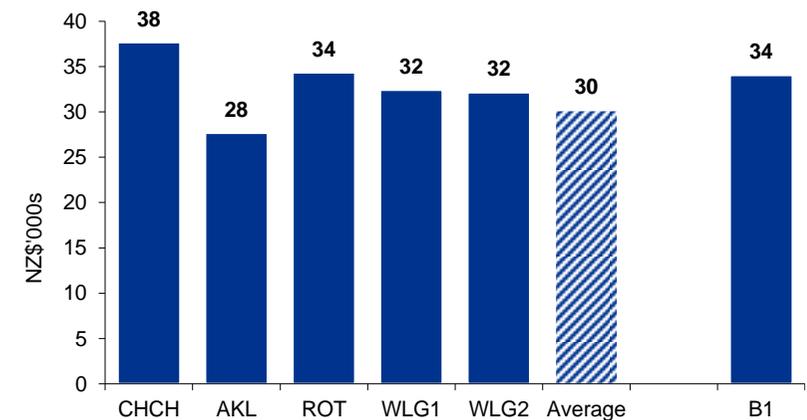
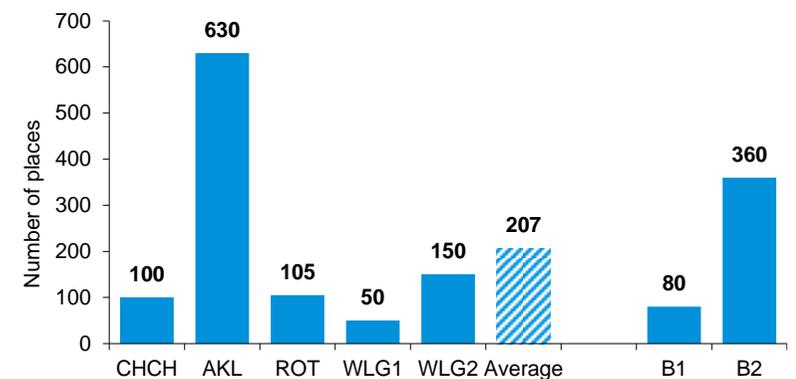


Diagram: Number of outcomes per provider (over both years)



Housing First Cost to deliver analysis

The average cost split per provider shows that the cost of delivering HF services is largely driven by staffing costs and property costs, which make up 48% and 23% of total costs, respectively.

HF cost templates: Average cost split

Four out of five of the pro-forma cost templates include cost of establishment in the first year of contracting, ranging between NZ\$67k and NZ\$298k. The establishment cost varied depending on items included under this category. In some cases, establishment costs included salaries, furniture, IT, training or recruitment of staff, cost for engagement with stakeholders and advertisement, such as website development, social media cost or branding. These costs were excluded from the average cost per outcome split to give a better reflection of average operational cost once the program was established.

The comparison shows that the main cost drivers across all five providers are staffing costs (48%) and property costs (23%), however the five pro-forma cost templates show varying assumptions in terms of:

- Amount and commencement months of staff members, assumptions regarding the staff to client ratio and the required specialist roles,
- Property costs, such as annual cost assumptions related to setting up client houses, meth testing or repairs/ maintenance, and
- The composition of other cost items, as some providers may allocate staffing costs differently (i.e. into overhead)

We note that the benchmark data reflects a higher proportion of staffing cost than the five pro-forma cost templates. Furthermore, the pro-forma cost templates reflect a higher proportion of overhead costs than the benchmarks, although the submitted pro-forma are broadly consistent (9-15% of total costs).

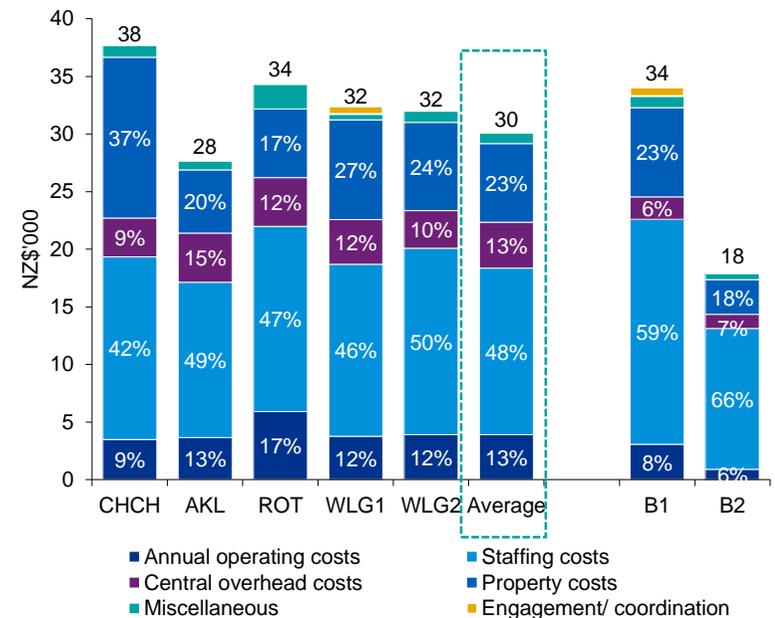
Comment on HF costs

While we have sought to compare costs between providers and the HUD benchmarks, we do not have independent benchmarks to compare the reasonableness of costs submitted by providers.

HF is a relatively intensive and high-cost intervention over and above any support a Public Housing tenant would receive from their Public Housing provider. We also note:

- The costs per outcome across providers is broadly similar, indicating a level of consistency in the contracting approach for HF thus far.
- The breakdown of costs is similar across providers, although the different formats of the cost pro-formas (i.e. inconsistent naming conventions for staff types, some pro-formas did not include FTE counts) means that the scope to compare differences in business models using the data is limited.

Diagram: Average cost split per provider (over two years)



Housing First Expenditure trends

Housing First was first funded in Budget 2017 and received increases in subsequent Budgets, which is reflective of the ongoing roll-out of HF across the country.

There was only one provider collective in Auckland in the first year. Subsequently, HUD has contracted providers in additional locations.

HF service component

HF was first funded in Budget 2017. The appropriation for HF is specifically for the wrap-around services provided to clients, and does not include the associated accommodation costs for those clients that are housed in Public Housing (which sit within the regular IRRS appropriation).

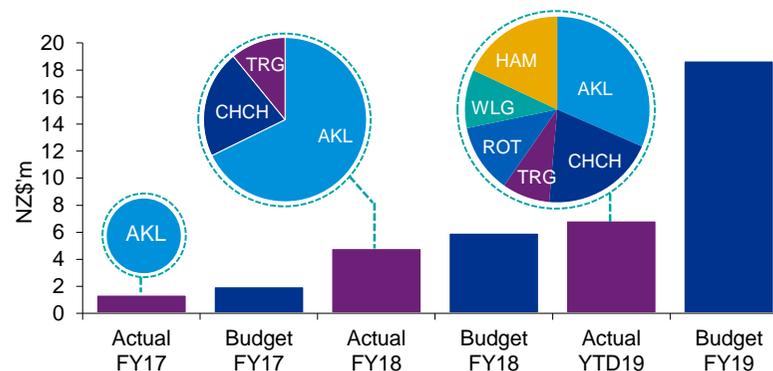
HF has received increases in the subsequent two Budgets. The total appropriation amounts available included intra-year increases and carry-forward amounts underspent during the ramp-up of the program.

The total appropriation amounts versus the actual have been:

- A budget of NZ\$2.0m in 16/17, of which NZ\$1.4m were spent,
- A budget of NZ\$6.0m in 17/18, of which NZ\$4.8m were spent, and
- A budget of NZ\$17.8m for 18/19 (including additional budgets), of which NZ\$6.9m was spent as at 30 April 2019 (YTD19). We were informed that the most recent actual as at 30 June 2019 was NZ\$17.5m and included significant cash-outflows in May and June.

The diagram below shows the budget amounts as well as the actual amounts spent, the latter are split by location.

Diagram: Funding actuals and budget per year



The contracts between HUD and the HF providers have individual contract starting dates and, thus, may not be consistent with HUD's financial years. We have not sought to reconcile the cost in the prepared pro-forma cost templates (individual contracting period) with the appropriations (financial year). Note some contracts also include separate payment agreements related to methamphetamine remediation.

Accommodation costs associated with Housing First

The majority of HF clients are in IRRS housing, predominately in CHP Public Housing. A significantly smaller number are in private rentals or HNZ properties.

While the IRRS appropriation does not specifically separate out HF clients, we have been provided with an estimation by MSD. This estimation is based on IRRS expenditure that went to tenancies marked as HF in the MSD data base.

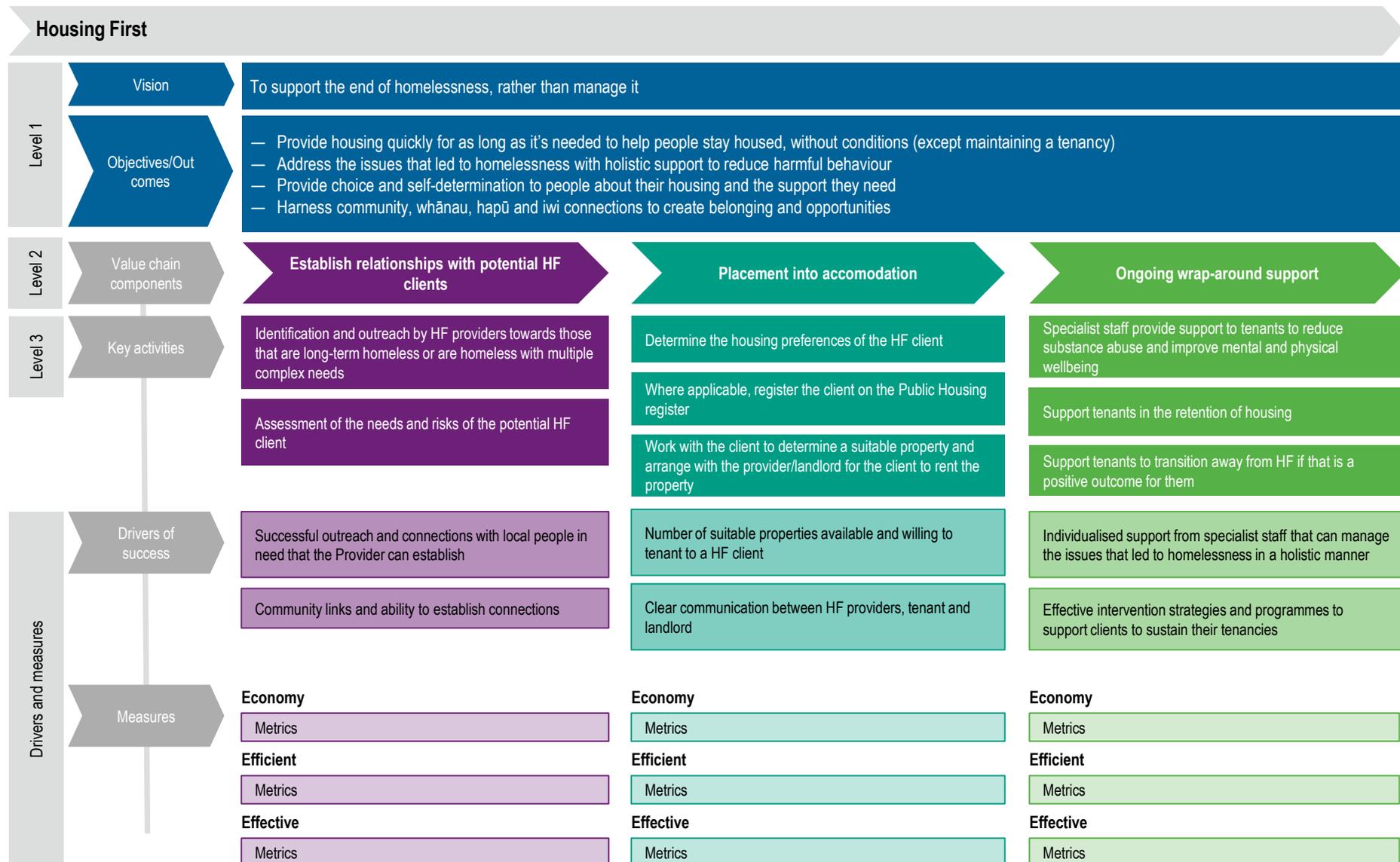
- For FY18, the MSD estimation shows IRRS expenditure of NZ\$1.2m. Together with expenditure for wrap-around services, the total expenditure for HF amounted NZ\$6.0m in FY18.
- Based on the above, 80% of the total expenditure for HF clients was spent on wrap-around services, while 20% was spent on housing costs.

Actual cost per outcome

The contracted payment amount for wrap-around services is derived with reference to the number of contracted outcomes and "maintenance clients" as opposed to the actual number of outcomes generated within the period. Based on this, we have not attempted to conduct an analysis of the cost per actual outcome, although we do discuss contracted versus delivered outcomes further later in this section.

Housing First Value framework

The following diagram provides a framework for considering the different components and activities of the supply of HF.



Housing First

Value for money discussion (1 of 3)

While reporting data has been inconsistent in the past, HUD has informed us that they have taken steps to improve reporting performance data in the future.

Introduction

As set out in section 3, our approach to value for money assessment is through considering key metrics across:

- **Economy:** The input costs incurred by HF providers
- **Efficiency:** The services provided by HF providers given the level of inputs
- **Effectiveness:** The effectiveness of the HF provider in achieving the programme's objectives.

The above value for money analysis is not to consider whether the overall social and economic benefits of the HF intervention exceed the costs of homelessness. It is not intended to be an economic cost-benefit analysis of the programme to assess the overall societal benefit of a reduction in homelessness. Rather, given the government's objectives, value for money analysis considers the evidence whether these are being achieved at an appropriate cost.

Potential value for money metrics

We have not developed a detailed set of value for money metrics for HF, but do indicate below the types of metrics we believe would be valuable for HUD to further develop for HF.

A key challenge in interpreting these metrics is developing relevant benchmarks on which to compare results. The nature of the programme should allow measurement across providers and over-time, as well as comparisons with similar international programmes.

Economy

- FTE cost by staff type.
- Ratio of cost types (e.g. overhead, staff, property).

Efficiency

- Number of FTEs per new client (housed and yet to be housed).
- Number of FTEs per maintenance client.
- Cost per annum per tenant (recruitment and housing placement).
- Cost per annum per maintenance client (across different intensity levels).
- Ratio of contracted places to actual places.

Effectiveness

- Proportion of tenants meeting the programmes target cohort .
- Measures of improvements in tenant well-being (i.e. reduction in substance use).
- Retention within the programme, housing outcomes and graduation rates.
- Tenant feedback (e.g. extent to which tenants feel supported, extent to which tenants report improved community connections).
- Sustainability of post-programme housing outcomes (i.e. the extent to which former HF clients maintain a housing outcome following programme graduation).

Housing First Value for money discussion (2 of 3)

HF providers are required to report on client details and high-level programme outcomes.

While the data set is subject to inconsistencies, it forms the basis for initial high-level performance analysis.

HF performance data

HF providers are contracted to deliver a certain amount of outcomes over a certain period and to report on quantitative and qualitative aspects of their delivery. We have been provided with the reported data as at 31 March 2019. The current data collection includes information on:

- Client details (e.g. age, gender, homeless duration).
- Current housing status (i.e. currently housed, previously housed, no longer housed by HF).
- Current programme status (i.e. continued support, withdrawn, graduated).

As part of our work, we understand that the HF data collection hasn't necessarily been consistent between providers thus far, and therefore analysis for this report is relatively limited. In particular, we have not presented HF cohort data. We understand that HUD has actively taken steps to resolve some of its data concerns which will be available in coming months. Further, there is not currently a reliable mechanism to link the performance data with cost data.

Results and commentary

- Since inception, there have been 1,224 individuals engaged with HF providers. Of these, 1,064 individuals were accepted into the programme, with a further 73 pending.
- Approximately 78% of the individuals accepted into the programme since inception remain in the programme, while the remaining 22% are no longer part of the programme.
- Of the 1,064 individuals accepted into the programme, 522 are currently housed, 197 are not currently housed (but were previously housed), while the remaining 345 are yet to be housed for the first time. In other words, approximately half of the individuals within HF are currently in housing.

Diagram: Client housing status by provider (as at 31 March 2019)

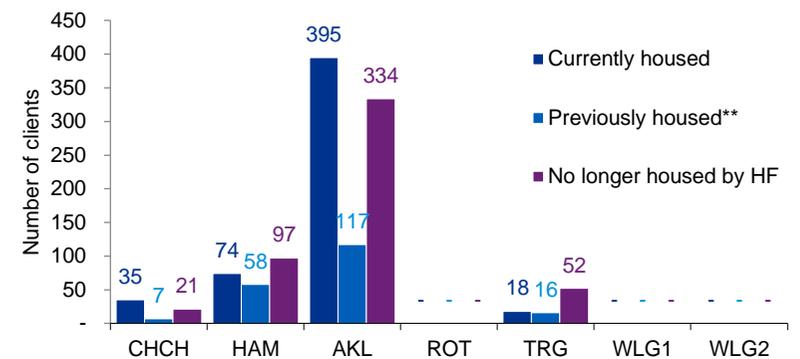
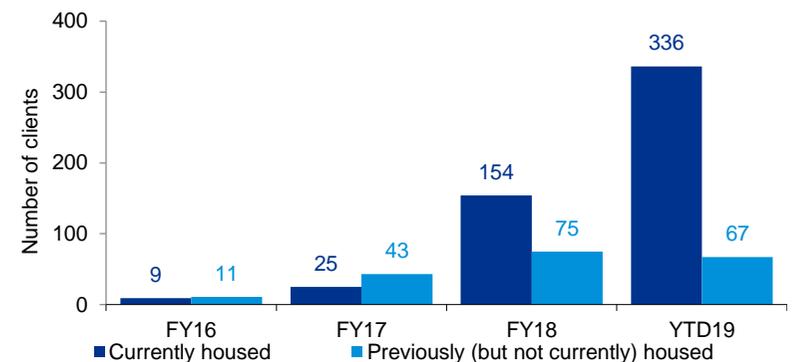


Diagram: Number of outcomes per financial year



Housing First

Value for money discussion (3 of 3)

As the programme expands, there is scope to further evolve data collection to improve performance analysis in the future.

Results and commentary (continued)

- The 22% of accepted clients who have left the programme represents 239 individuals or whānau. As shown in the diagram to the right, the majority have withdrawn from the programme, with a small number having graduated or died.
- The scope to match up the number of delivered outcomes relative to the contracted is limited given available data. While this is indicative only, the data suggests that the number of delivered outcomes is generally lower than the contracted amounts.
- The data collection focuses on housing outcomes, and therefore does not provide an indication of the wider potential impacts of the programme (i.e. other tenant wellbeing measures).

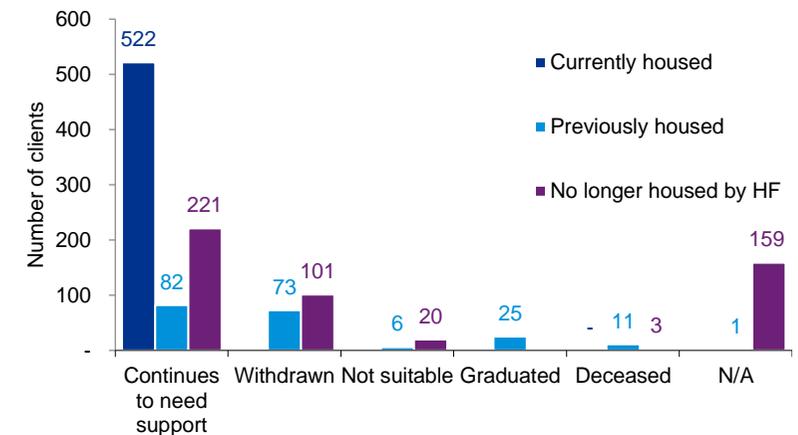
Academic research¹ published in 2019 considered outcomes from a HF programme run by the People's Project in Hamilton. The paper used the Integrated Data Infrastructure (IDI) to consider the usage of government services by HF clients. The report found that HF clients had a significantly greater number of interactions with government services (such as health, justice, welfare) relative to the general population, prior to homelessness. The authors considered this evidence the social support systems still fails some of society's most vulnerable, as well as providing a baseline for future HF evaluation.

Next steps

Based on our high-level analysis, we would suggest that:

- As contracts are renewed, providers complete standardised cost templates that allow more detailed comparison of key inputs (e.g. staff level, type) and understanding of alternative business models.
- HUD ensure systems and reporting allows the monitoring of the delivery of actual outcomes relative to contracted levels.
- HUD continue to improve the process for data collection from providers to enable reliable analysis.
- HUD to continue to consider broader data collection measures focused on tenant wellbeing and reduction in risk factors.

Diagram: Current service and housing status



Note: N/A status represents cases where current service status was not included in the dataset

Table: Service status by housing status (tenants accepted but no longer in programme)

Service statuses	Number of clients	% of total
Withdrawn	174	73%
Not suitable	26	11%
Graduated	25	10%
Deceased	14	6%
Total	239	100.0%

Table: Estimated actual relative to contracted delivery

Comparison of contracted versus delivered outcomes							
Outcomes	CHCH	HAM	AKL	ROT	TRG	WLG1	WLG2
Period	12 months	8 months	2 months	New provider, no client data yet	12 months	New provider, no client data yet	New provider, no client data yet
Contract	50	51	33		50		
Delivered	42	48	42		34		

9

Transitional Housing

Transitional Housing Introduction

Transitional Housing is a programme focused on providing short-term housing for those who urgently need a place to stay. TH is tailored to support the transition to long-term housing options.

Background to TH

Transitional Housing (TH) is focused on providing short-term accommodation for those who don't have somewhere to live. TH is based on a 24 week programme, on average, consisting of:

- 12 weeks accommodation and support services in temporary transitional housing (or longer, if required), and
- 12 weeks follow-on support once the tenant has found more permanent accommodation (not available for contracted motel places).

The expected level of support services includes tenancy and broader support services, as well as identifying, and assisting a household to secure and move into, long-term housing.

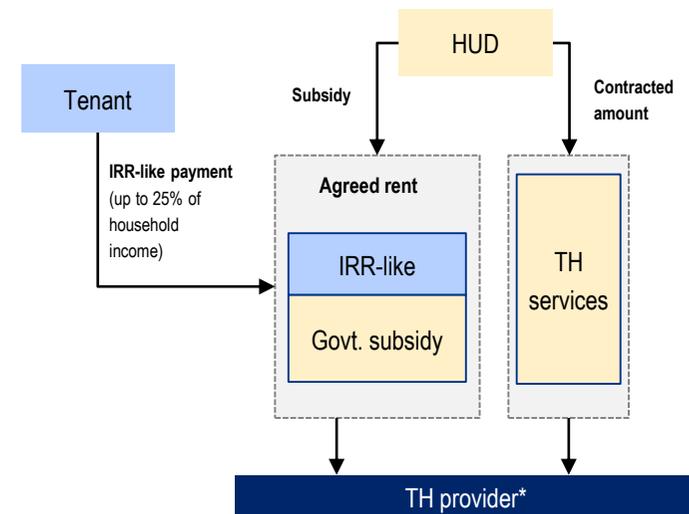
Potential TH clients will have been assessed by MSD as having the greatest priority, e.g. in cases where clients have been living with family, in overcrowded or in sub-standard accommodation and can no longer stay there.

TH funding model

TH providers enter into separate contracts with HUD for the provision of housing places and, in most cases, for associated service provision. The funding of accommodation is based on actual occupancy while the funding of services is based on an anticipated level of services.

Some accommodation is provided by motel operators. In these cases, the service component is usually provided by a separate (long-term) TH provider. However, a small number of motels provide services to TH clients.

Diagram: High-level funding flows



* = May be two different providers, e.g. in cases where a motel provider is contracted to provide accommodation and another TH provider is contracted to provide services.

Transitional Housing

Contract arrangements and scope of cost data

HUD requires TH providers to complete a cost template prior to contracting and to report on service outcomes for the duration of the contract.

TH funding model (cont.)

The funding for the accommodation component of TH consists of two components:

- TH tenants are required to pay an income-related rent which is modelled after IRR. Tenants are generally required to pay no more than 25% of their income.
- In general, TH providers receive 80% of the agreed rent from HUD, irrespective of the tenants' level of contribution. Potential overpayments to the TH providers are intended to cover for low occupancy periods or cases of a below average contribution by the tenant.

The funding for TH services is derived with reference to the number of anticipated clients and respective services.

Contract arrangements for TH

TH providers enter into separate contracts with HUD for the provision of TH places and, in most cases, for associated service provision. As a part of these agreements, HUD requires TH providers to report on service outcomes, including:

- The successful identification of a sustainable housing solution for all households leaving TH.
- An average occupancy rate of 90%,
- An average stay (of a household in a TH place) for 12 weeks, and
- At least 10% of households leaving TH accessing sustainable housing in the private rental market.

Scope of data

Expenditure data

Thus said, we have sought to analyse the expenditure trends based on the following information provided:

- Funding data (Payments from HUD to TH providers) for FY17, FY18 and FY19, split by:
 - Provider (separated and grouped by long-term and motel providers).
 - Region.
 - Accommodation and services component.
- Monthly amounts of TH places, split by region and by long-term versus motel providers

Performance data

We have not independently analysed performance data as part of this report. Our comments are based on previous analysis by MSD that provided a detailed summary of what data is available. We therefore did not seek to replicate that work.

Cost data

As part of procurement and contracting, TH providers must complete a cost template setting out the level of resources they require. This is based on:

- The expected number of households receiving accommodation and/ or services.
- Annual estimated property rental costs.
- Annual tenancy management and service delivery cost estimates, such as personnel, overheads, vehicle lease costs, utilities and cleaning.

We were provided with six examples of populated TH cost templates. We have not reported results from these given the small sample size.

Transitional Housing Funding and expenditure overview (1 of 3)

TH was first funded in Budget 2017, with higher provided in the subsequent years reflecting the growth of the programme.

At 30 April 2019, there were approximately 2,734 TH places.

Funding of TH

TH was first funded in Budget 2017. The funding for TH is provided through three main appropriations:

- TH services, for the wrap-around services provided to TH clients, totalling NZ\$49.4m in 2019/20.
- Provision of TH places, for accommodation costs, totally NZ\$65.5m in 2019/20.
- Loans to support the acquisition, development or construction of additional TH places.

In addition, there is an appropriation related to impairment of TH assets.

Expenditure trends

The second table on the right provides a regional breakdown of TH places and funding. Note that the annual funding data shows actual expenditure based on cash-outflows and therefore differs from the appropriation information above .

Based on this high-level expenditure information:

- TH expenditure has grown significantly between FY18 to FY19.
- Approximately 42% of places are in Auckland, which has been broadly consistent across years.
- Services provided by TH providers accounts for approximately 42-46% of the total cost of the programme.
- As discussed in further detail on the following pages, the proportion of TH accommodation provided through motels have increased each year of the programme.

Summary - Transitional Housing appropriation			
NZ\$'000s	FY17	FY18	FY19
TH Services	6,768	36,771	49,438
Provision of TH Places	1,363	35,432	65,452
Subtotal	8,131	72,203	114,890
Impairment of Crown Assets Relates to TH	0	2,555	0
Acquisition, Development and Construction of TH	100,000	0	84,568
Total appropriation	108,131	74,758	199,458

Summary - TH funding and number of places by region						
	Number of places (as at month-end)			Annual amount of funding (in NZ\$'000s)		
	Jun-17	Jun-18	Apr-19	FY17	FY18	FY19
Auckland	470	949	1,136	2,006	29,906	50,634
East Coast	60	252	273	75	7,159	15,196
Bay of Plenty	44	199	264	174	5,380	9,688
Wellington	125	209	243	526	3,248	9,196
Canterbury	165	272	302	911	6,645	8,185
Northland	102	139	157	452	2,255	5,162
Waikato	54	112	116	174	2,507	3,750
Central	33	60	81	100	1,396	2,821
West Coast Tasman	20	63	65	5	1,793	2,575
Southern	38	67	78	33	882	2,364
Taranaki	12	19	19	50	936	1,179
Total funding	1,123	2,341	2,734	4,505	62,107	110,749
Thereof						
Services in %				14.9%	46.2%	42.3%
Accommodation in %				85.1%	53.8%	57.7%
Thereof						
Long-term providers in %				98.0%	65.5%	57.4%
Motels (incl. services to motel clients) in %				2.0%	34.5%	42.6%

Note: We were provided with the monthly number of places between September 2016 and April 2019. We have extrapolated the number of places at April 2019 (YTD19 - 10 months) to June 2019 (FY19 - 12 months), using the average monthly growth across the last 10 months.

Transitional Housing Funding and expenditure overview (2 of 3)

The split of expenditure by long-term providers and motels shows an increase in the proportion of motels from 34% of total funding in FY18 to 43% in FY19.

In comparison, the level of motel places made up 27% of all TH places in FY19.

The over-proportionate funding reflects the higher cost of motel accommodation.

Diagram: TH funding split Auckland and Rest of New Zealand

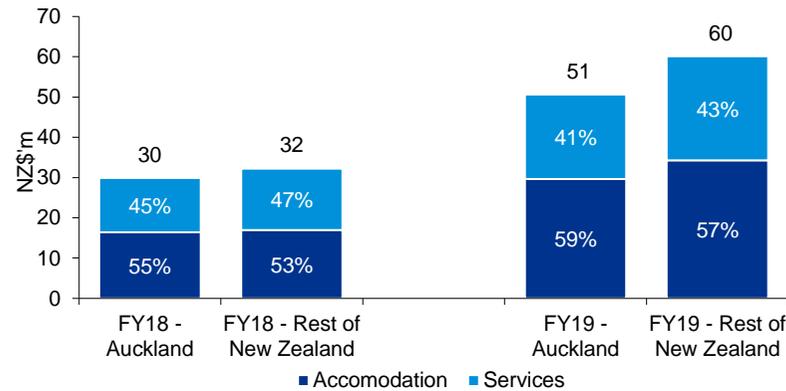


Diagram: Funding by region (for Rest of New Zealand)

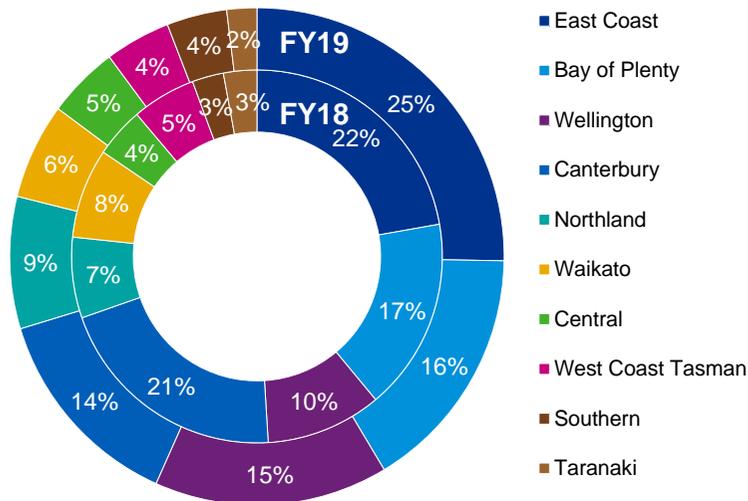


Diagram: TH motels' proportion of funding and places (FY19)

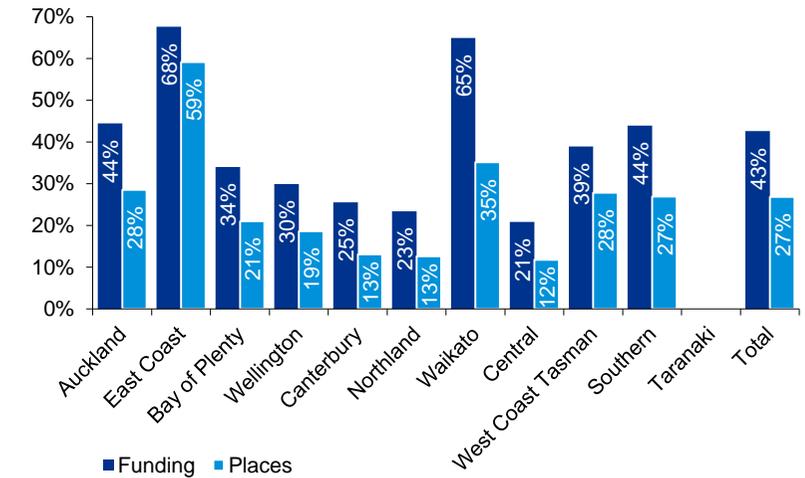
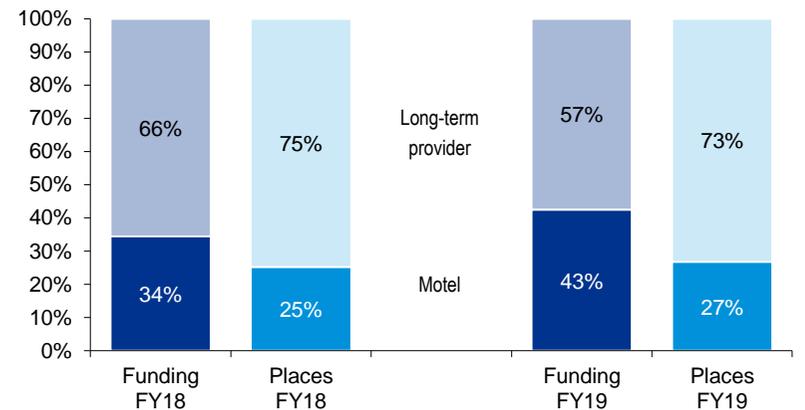


Diagram: TH funding and places split by motels/ long-term providers



Transitional Housing Funding and expenditure overview (3 of 3)

The average monthly cost for a motel place was NZ\$5.6k in FY19, which is more than double the cost of NZ\$2.7k for a long-term place.

While average cost of accommodation is significantly higher for motels than for long-term providers, the average cost of services for motel clients is slightly lower.

Cost per place (monthly)

We have sought to analyse the monthly average costs per place for FY18 and FY19, split by regions, accommodation and services and by long-term-providers and motels.

- The average monthly cost per place has increased from NZ\$2.7k in FY18 to NZ\$3.5k in FY19. The average monthly cost for a motel place was NZ\$5.6k in FY19, which is more than double the cost of NZ\$2.7k for a long-term place (FY18: NZ\$4.4k and NZ\$2.2k, respectively).
- While three regions show stable or slightly decreasing average cost, most regions show significant cost increases, with Wellington, Northland and Southern increasing most significantly

TH acquisition loans

There is a TH appropriation relating to loans to TH providers, largely to HNZ, to support the acquisition, development or construction of additional TH places.

There are two loan agreements related to the TH appropriation:

- A loan of NZ\$127.3m to HNZ, which has been drawn down in four parts. A further request was lodged for approval on 13 May 2019 to increase the loan facility limit to NZ\$153.2m.
- A loan of NZ\$8.7m to Monte Cecilia Housing Trust, which was approved to facilitate the redevelopment of a property for transitional housing purposes. There has been one draw down of NZ\$4.9m on this loan facility to date (draw down date: 30.05.2019)..

Diagram: TH funding split by long-term providers and motels

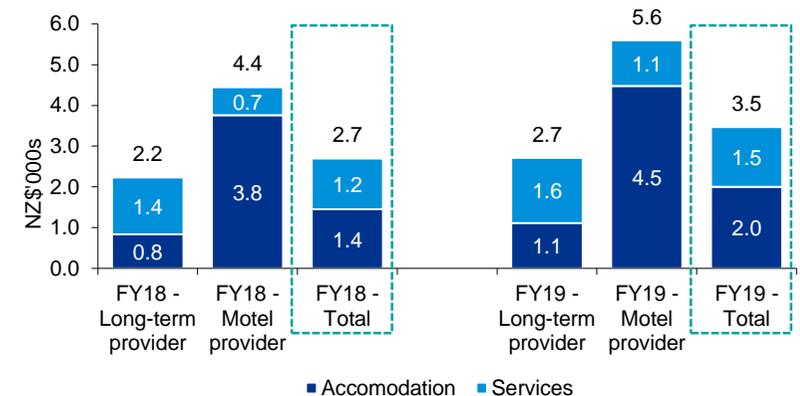
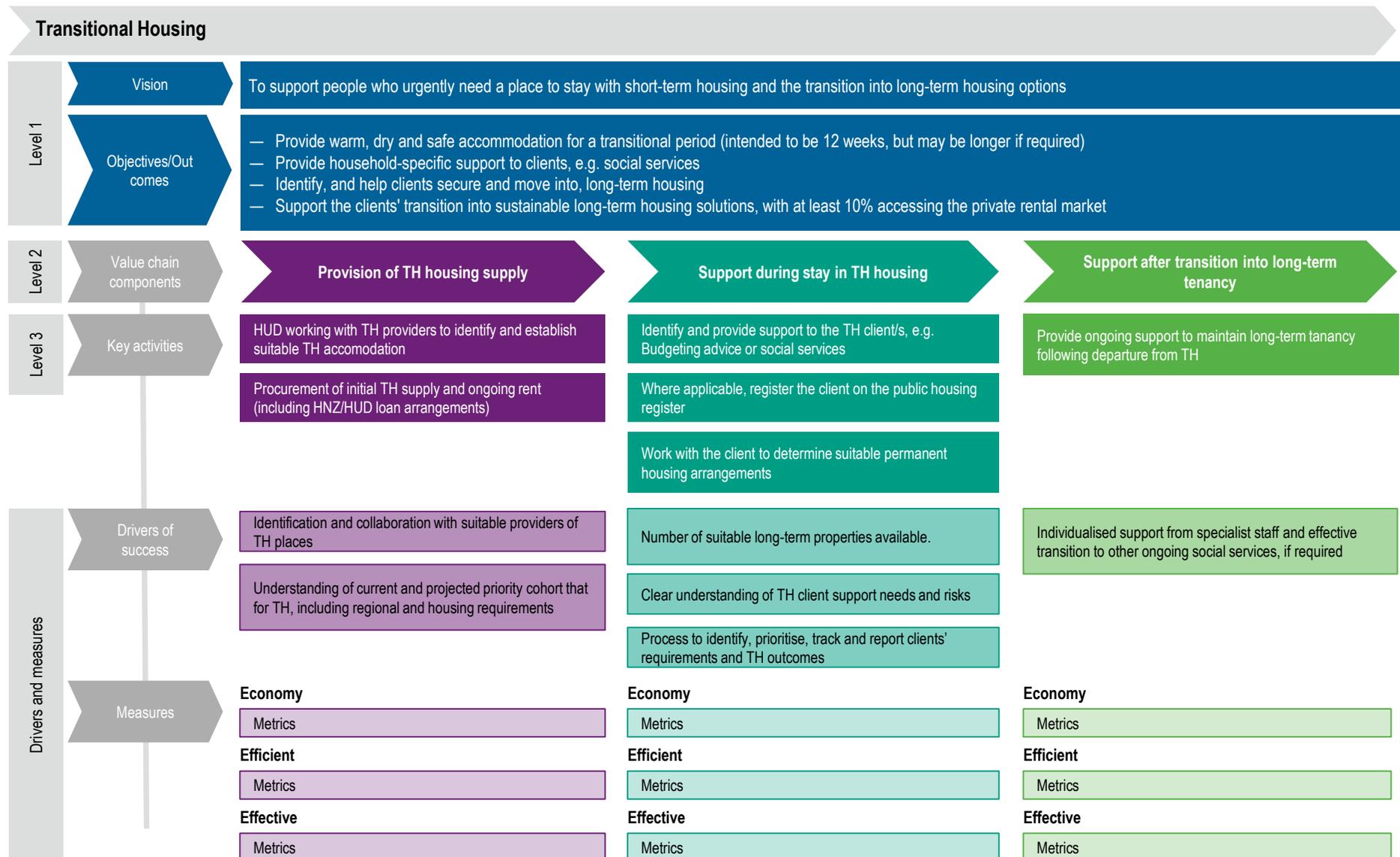


Diagram: TH acquisition loan status HNZ

Amount	Draw down date	Maturity date
NZ\$ 72.5m	20 June 2017	20 June 2022
NZ\$ 22.5m	26 June 2017	20 June 2022
NZ\$ 23.4m	2 August 2018	20 June 2023
NZ\$ 8.9m	30 November 2018	30 November 2028

Transitional Housing Value framework



Transitional Housing TH value for money

The Transitional Housing Annual Performance Report prepared by MSD for presents operational performance metrics across TH providers.

The report highlights issues with data quality, consistency and the suitability of the performance metrics that providers are requested to report.

TH annual report

We have been provided with Transitional Housing Annual Performance Report (June 2017 – June 2018). The report was prepared by MSD and is intended to be initial exploratory work of available data rather than serve as a definitive evaluation of TH performance. In particular, MSD is not in a position to verify the data collected, and noted that the data “varied widely in its consistency and quality across the period”.

Summary results

- *Occupancy (as measured by proportion of time a household is in residence in a contracted place):* An overall occupancy rate of 88% for the year, with relative consistency across household size and region.
- *Average stay for exited tenants:* An average stay of 10.6 weeks for those that have exited, relative to an expectation of 12 weeks. This was positively correlated with exit reason (i.e. more positive outcomes such as moving into own home or Public Housing was correlated with longer average stay lengths). There was significant provider variation, although this may be due to different place types.
- *Average stay for still in service tenants:* At the end of the reporting period, the average stay for tenants in service was 22.4 weeks, including 45 households still in the programme for over a year.
- *Exit reasons:* Of the 5942 households assisted during the period, 2878 exited from transitional housing. Of the exits:
 - 44% of exits were positive (i.e. Public Housing, private rentals).
 - 25% were to hospital, family, other providers or non-TH motels or boarding houses.
 - 31% ‘low efficacy’ exits, where the reason is stated as unknown, removed from service or arrested.

- *Turnover:* The data suggests that, although average stay is around 10 weeks, this is being brought down by short-stay high-turnover situations (i.e. the 10 week figure masks households who have stayed much longer than this). For places where an exit occurred, almost 70% of places had no more than 3 households over the year.
- *Low efficacy exits:* A more detailed analysis of these exits indicate that no reason was given in the majority of cases.

The annual report notes the key limitations with the current data collection and analysis:

- Inconsistent completion of templates by providers, variable quality and levels of compliance.
- A lack of connection between performance metrics and cost data.
- A wide variation in service levels and models used by providers which are not visible to government agencies.

Comment

TH to date has largely focused on a supply strategy with priority given to increasing the number of places available. As the programme matures, there is the opportunity to consider comparative outcomes from TH service provision across providers, cohorts and intervention approaches.

Given the annual report provides a reasonably detailed analysis of TH performance data, and we were informed that further data was not available, we have not sought to replicate that work given the annual report appeared to reasonably comprehensively analyse what data is currently available. We support the recommendations set out in that report for the future development of performance monitoring for TH.

10

Community Group Housing

Community Group Housing Introduction

CGH provides support to CGs, which deliver services to specific target cohorts.

Background

CGH provides support to Community Groups (CGs) to deliver their services to their target clients, particularly where the provision of that service requires residential housing. For example, CGs support:

- people who experience mental or psychiatric illness.
- residential alcohol and drug services.
- people seeking refuge.
- prisoner reintegration.

To be eligible for CGH support, a CG must be contracted to provide residential services (such as those listed above) and have appropriate governance, management structures and accreditation.

The CGH programme is managed by HNZ, which works with the CGs to identify, modify and provide suitable properties. The key relationship in CGH is between the CG and HNZ. There is no direct relationship between the eventual 'tenant' of the residential property and HNZ.

As at 31 March 2019, there are approximately 1,500 properties that fall within the CGH programme.

CGH funding model

There are two primary operating funding flows associated with CGH:

- HNZ enters into an agreement with a CG which, historically, have been for a concessionary rental amount below the market rent for the property. HNZ is reimbursed for this difference, referred to as the **market rent top up**.
- CGs may apply for a subsidy to allow them to meet the level of agreed rent charged by HNZ, where they can demonstrate that they cannot meet this payment from their other funding sources. This is referred to as the **rent support subsidy**.

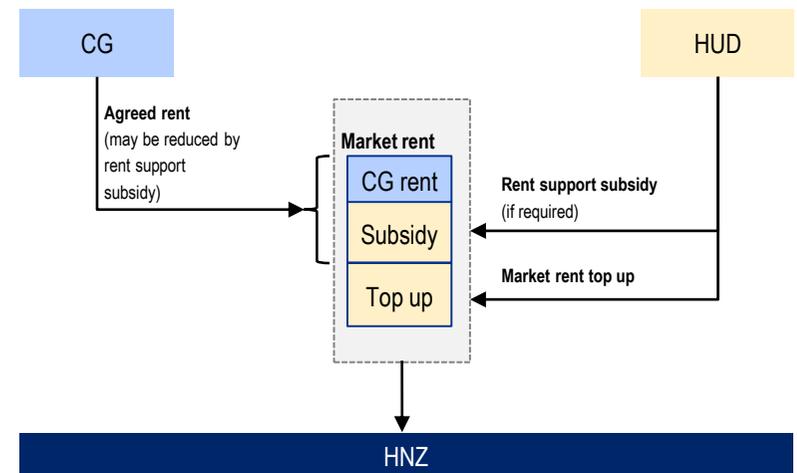
CGH funding model (continued)

These two funding flows are not cumulative per se. The rent top up is funding to HNZ, while the rent support scheme is effectively funding to the CG.

In addition, HNZ works alongside HUD and the CGs to acquire new properties for use as CGH. For this purpose, HNZ receives additional funding through an appropriation for new CGH supply.

Further detail of these arrangements is provided on the following slide.

Diagram: High-level funding flows



Community Group Housing Contract arrangements and scope of data

Historically, HNZ has entered into concessionary rental arrangements below the market rent and thus, received an appropriation for a market rent top up.

CGs can apply for a rent support subsidy to meet the agreed rent.

CGH contracting arrangements - overview

Through the CGH programme, HNZ supports eligible CGs to identify and rent a suitable property. Historically, HNZ has entered into concessionary rental arrangements below the market rent and thus, received an appropriation for a market rent top up.

Where a CG can not cover the payment of the agreed rent, the CG is able to apply for rent support subsidy. Depending on the nature of the CG service, this can be:

- Rent support of up to 70%, if the CG provides support for people in residential supported living situations, and
- Rent support of up to 90%, if the CG provides support for family, welfare and respite services (both residential and non-residential).

It is our understanding that HNZ is generally aiming to reach market rent agreements with CGs in the future, which would give both HNZ and the CG more transparency regarding the financial support the CG receives.

Funding of new supply

HNZ works with the CG to identify their requirements and to find a property that meets the needs of the clients or customer groups the CG supports. Depending on the CG, the property may require modifications to accommodate the CG's and their customers' needs. HNZ receives an appropriation to purchase and modify new supply of properties and to maintain the existing portfolio.

Scope of data

We have sought to analyse expenditure trends related to CGH based on the following information provided:

- A full data set of all CGH properties and rent-related funding, split by:
 - Months between April 2014 and March 2019,
 - Weekly market rent top up, rent support subsidy and CG rent,
 - Typology, and
 - Regions.

We have sought to analyse the data set at the respective year-ends of FY14 to FY18 (as at 30 June) and YTD19 (as at 31 March 2019). Note that we received monthly property information, which included weekly rent and rent-related funding information, but did not include a reconciliation to the annual funding.

The data set provided included both property and land information. Properties are distinguished by their rental status, which can be occupied, void or closed. For the purpose of our analysis, we have analysed the rent-related funding for occupied properties at each respective year-end. This is based on the assumption that void or closed properties would not receive funding. This means that the amount of properties reflected in the analysis may be lower than the managed stock, which may include void or closed properties.

Community Group Housing Property portfolio trends

The CGH portfolio is largely made up by properties with six or fewer bedrooms, however it includes properties with up to 18 bedrooms.

The portfolio includes 1,471 occupied properties at 31 March 2019 and showed relatively minor fluctuation across the period.

Summary of the CGH portfolio

As at 31 March 2019, the data set showed 1,471 occupied properties nationally which is largely consists of residential tenancies and includes a small number of non-residential leases.

The portfolio consists of individual properties which are often modified to suit CG needs. More than half of the portfolio is made up of 1-, 2- and 3-bedroom properties and more than 90% of the portfolio are 1- to 6-bedroom properties. The largest property in the CGH portfolio has 18 bedrooms.

Over the period under review, the balance of properties in the portfolio did not show significant movement. The chart on the bottom right chart for shows intra-year additions and reductions to/from the portfolio of occupied properties. Additions may include new CGH supply (e.g. property acquisitions or additional lease agreements) or a new tenancy of an existing CGH property that has previously been void. Reductions are driven by a property becoming void (unoccupied) or closed.

The chart below reflects the occupied CGH portfolio by region. Note that 50% of the portfolio are located in Auckland, Wellington and Canterbury.

Diagram: Summary of occupied CGH portfolio by region (YTD19*)

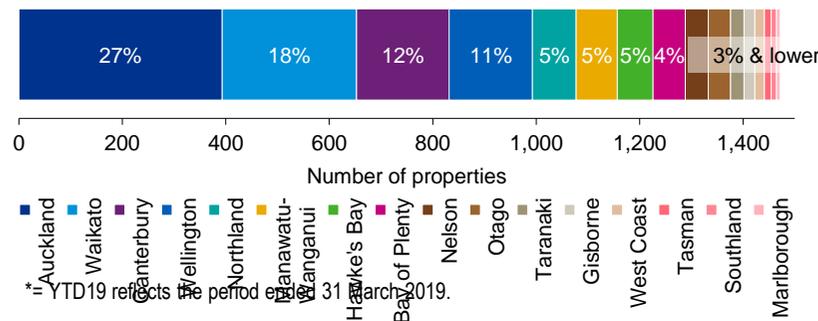


Diagram: Summary of occupied CGH portfolio by typology (year-end*)

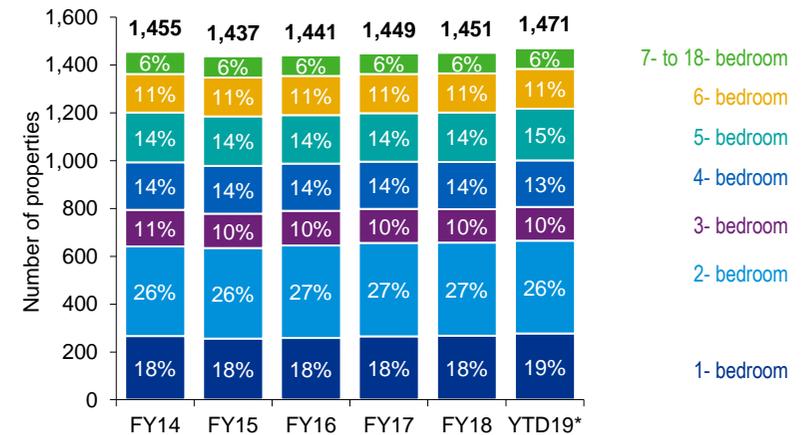
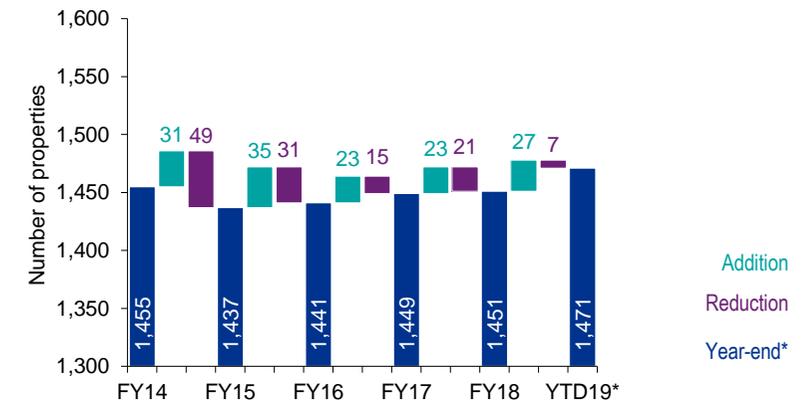


Diagram: Addition/reduction of occupied CGH portfolio



Community Group Housing Expenditure trends (1 of 2)

At 31 March 2019, approximately half of market rent for CGH was paid by the CG's, while the other half was funded by government.

Expenditure trends - rent

The expenditure related to CGH is largely driven by the market rent defined by HNZ, which is then partly funded by appropriations and partly by the rent payments received from CG.

At YTD19 (31 March 2019), the average funding of occupied places was driven by:

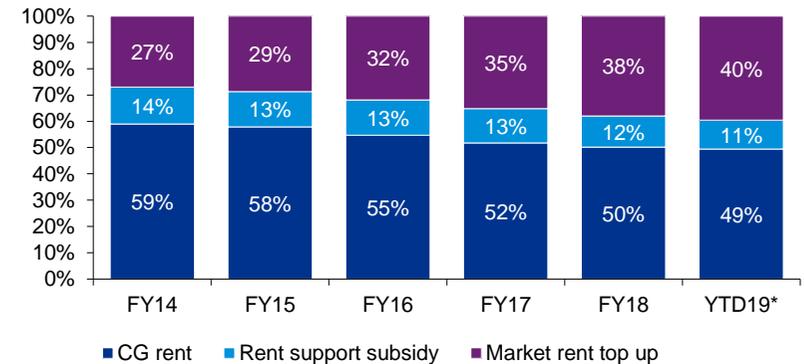
- 49% of **CG rent** (after rent support subsidy).
- 11% of **rent support subsidy**, which is intended to subsidise CG's that are unable to meet the agreed rent.
- 40% of **market rent top-up**, which is intended to cover the difference between agreed rent and market rent.

It is our understanding that HNZ aims to increase the level of agreed rent to the level of market rent and, thus, aims to agree market level terms for both new and existing lease agreements with CGs. In the long-term, this would shift required funding from market-rent top-ups to rent subsidies.

We have not sought to request or analyse any further funding which CG's may receive from other sources, including potential government funding.

Note we have sought to gross up the weekly funding picture to approximate annual amounts and were able to broadly reconcile the information to the annual appropriations.

Diagram: Summary of funding proportions of market rent



* = YTD at 31 March 2019 (9 months).

Summary - Average (one week) market rent per property at year-end

NZ\$	FY14	FY15	FY16	FY17	FY18	YTD19*	CAGR
1- bedroom	184	196	209	222	236	253	6.6%
2- bedroom	267	290	308	325	348	364	6.4%
3- bedroom	327	353	368	394	422	441	6.2%
4- bedroom	412	432	453	481	518	539	5.5%
5- bedroom	467	494	514	541	574	596	5.0%
6- bedroom	502	549	557	587	621	637	4.9%
7- bedroom	588	623	645	674	714	753	5.1%
8- bedroom	604	634	651	700	695	776	5.1%
9- bedroom	628	637	619	624	633	653	0.8%
10- bedroom	765	853	843	888	917	983	5.1%
12- bedroom	1,200	1,200	n/a	n/a	n/a	n/a	n/a
17- bedroom	1,360	1,400	1,400	1,470	2,300	2,300	11.1%
18- bedroom	2,600	2,625	2,725	2,795	3,105	3,240	4.5%

* = YTD at 31 March 2019.

Community Group Housing Expenditure trends (2 of 2)

The total appropriation for CGH includes rent-related funding as well as funding for new supply of CGH properties.

Funding for the market rent top up has increased to NZ\$14m for Budget 2018/19, while the appropriations for rent support subsidy and new supply remained static.

Expenditure trends – total appropriation

Funding for CGH is provided through three main appropriations:

- Market rent top up, totalling NZ\$13.9m in 2018/19
- Rent relief, totalling NZ\$4.1m in 2018/19
- Funding to support the acquisition, development or construction of additional CGH properties, totalling NZ\$5.8m in 2018/19.

The increase of the annual appropriations for CGH was driven by additional funding for market rent top up while the appropriations for rent support subsidy and new supply remained relatively static.

Property modifications

HNZ seeks to provide CGH properties based on the requirements of the individual CGs. New supply is generated through the acquisition of existing or new (turn-key) properties as well as leasing of properties. Where existing properties are acquired or leased, HNZ may incur additional costs to make a property “fit for purpose”.

While the cost of property acquisitions was available, we were informed that additional modification costs are not captured separately. We have therefore not sought to analyse the average acquisition cost of new CGH supply.

Diagram: Summary of CGH appropriation

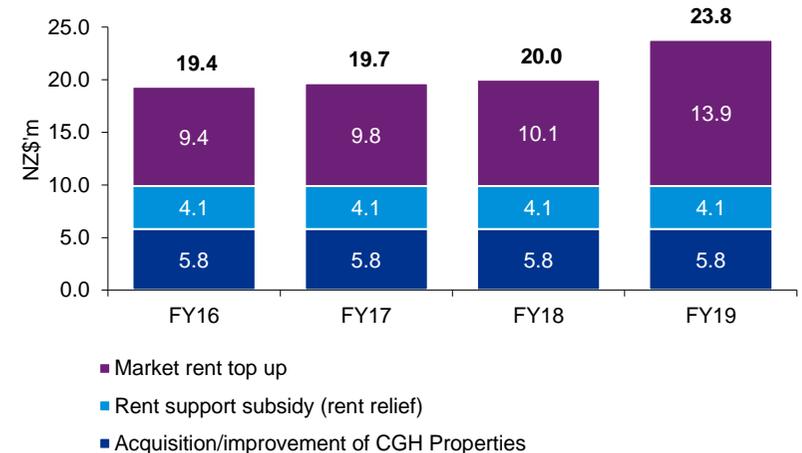


Table: Summary of new CGH supply

New CGH supply	FY17	FY18	YTD19*
Number of leased properties	7	24	0
Number of acquisitions	20	21	11
Total cost of acquisitions	NZ\$5.8m	NZ\$5.3m	NZ\$4.1m

Note that the number of (new) leased places and acquisitions relates to the total portfolio and therefore does not reconcile to the fluctuations of occupied places on page [xx].

* = YTD at 31 March 2019 (9 months).

Community Group Housing Discussion

While we have not considered CGH funding settings in depth, current arrangements do not appear to align responsibilities with agencies best placed to manage them, nor do they provide clear transparency as to the true cost of supporting particular cohorts.

Introduction

The funding and contractual arrangements for CGH are significantly different from those of Public Housing. Based on discussions with HNZ and previous work that HNZ has completed reviewing CGH funding, we note the following:

- HNZ is the provider of the property under Public Housing and CGH, but HNZ has no direct relationship with the tenant in CGH. Essentially the CG is the tenant and manages the relationship with the individuals living in the property. HNZ has no traditional tenancy management role.
- CGH funding arrangements appear to reflect an insufficiency of funding by the primary agency to cover the full costs of CGs in providing their services. In effect, HNZ is providing subsidies to support the delivery of services for which another agency has commissioned.
- CGH is based on a Residential Tenancy Agreement between HNZ and the CG, which provides 90 days notice to each party. This only provides very limited certainty to support development/investment for bespoke properties where CGs are unable to source appropriate properties in the private rental market.
- A review by HNZ in 2018 found inconsistency in the level of funding that some CGs were eligible to receive, and some CGs who were not necessarily eligible to access CGH support.
- There is inconsistency in the nature and level of funding between CGs, with some historical arrangements still in place. CGs therefore receive different levels of subsidy.

Comment

We have not considered the settings around CGH in depth, however we note that:

- The existing settings do not provide clear transparency and accountability of the full cost of funding services to support tenants in CGH. There are multiple subsidy streams across multiple agencies.
- The agency split creates an administration challenge given that HNZ only has limited knowledge of the CG's services and funding situation relative to the primary funding agency.

As a starting point, we are supportive of HNZ's current work to improve existing CGH arrangements, including:

- Shifting towards a more consistent rent setting approach for CGs.
- Assessing CGH providers to ensure that they meet eligibility requirements.
- Investigating shifting the rent top-up appropriation to the primary funding agency.