



## BRIEFING

### Further advice on a home ownership scheme to support KiwiBuild

<b>Date:</b>	24 September 2018	<b>Priority:</b>	Medium
<b>Security classification:</b>	In Confidence	<b>Tracking number:</b>	1064 18-19

Action sought		
	Action sought	Deadline
Hon Phil Twyford <b>Minister of Housing and Urban Development</b>	Agree recommendations.	12 October 2018
Hon Jenny Salesa <b>Associate Minister of Housing and Urban Development</b>	For noting.	N/A

Contact for telephone discussion (if required)				
Name	Position	Telephone		1st contact
Hilary Eade	Manager, Housing System Performance	04 901 8544	s 9(2)(a)	✓
Stephen Wenley	Senior Advisor, Housing System Performance	04 901 1352		

The following departments/agencies have been consulted
TPK, HNZ, Treasury, MSD. DPMC was informed.

Minister's office to complete:

☐ Approved

☐ Declined

☐ Noted

☐ Needs change

☐ Seen

☐ Overtaken by Events

☐ See Minister's Notes

☐ Withdrawn

Comments



## BRIEFING

### Further advice on a home ownership scheme to support KiwiBuild

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#### Purpose

1. This paper provides further advice on establishing a Government funded and administered home ownership scheme to support the sale of KiwiBuild houses. It seeks to clarify your core objectives, and provide design considerations and funding options for this proposal to enable officials to progress a bid for Budget 2019.

#### Executive summary

2. Despite existing government home ownership assistance, many renting households are unable to afford KiwiBuild homes due to insufficient income to service a mortgage and/or deposit. This raises the risk of there being insufficient first home buyers willing, eligible and able to purchase KiwiBuild homes when the programme reaches peak production in 2020/21.
3. On 6 September 2018, you asked officials to develop further advice on an option to establish a government funded and administered shared equity scheme to support the sale of KiwiBuild homes, including a potential bid for Budget 2019.
4. A shared equity scheme is a good fit for those on the cusp of being able to afford to service a mortgage on a KiwiBuild home, but is unlikely to be suitable for households further down the income spectrum. Such households would be supported by our complementary proposal for an Affordable Housing Fund.
5. To progress a shared equity scheme bid for consideration in Budget 2019, we need to clarify the Government's objectives for the scheme and identify possible funding parameters upon which costs can be modelled. How we design and target the scheme would have significant implications for the overall cost and for the number of households assisted.
6. Smaller shared equity contributions help households further up the income spectrum, who are likely to be closer to home ownership but could get there faster with shared equity assistance (households just above the median income, eg. income decile 6).<sup>1</sup> This represents a smaller cost to the Crown per household. Larger shared equity contributions reach further down the income spectrum (eg. income decile 5),<sup>2</sup> but represent a much higher cost to the Crown on a per household basis.
7. s 9(2)(f)(iv)

<sup>1</sup> Income decile 6 is a household income of \$80,200 to \$97,599 (*Household income and housing-cost statistics: Year ended June 2017*, Stats NZ).

<sup>2</sup> Income decile 5 is a household income of \$64,400 to \$80,199.

s 9(2)(f)(iv)

8.

s 9(2)(f)(iv)

9. Subject to your decisions on the advice in this paper, officials will report back to you with further advice to support the budget bid, including design of the scheme, eligibility and prioritisation criteria, and associated administrative processes.

### Recommended action

The Ministry of Business, Innovation and Employment recommends that you:

- a **Note** that this paper responds to your request on 6 September 2018 for officials to provide further advice on a Government funded and administered shared equity scheme to support the sale of KiwiBuild houses, including a potential bid for Budget 2019;

*Noted*

- b **Note** that smaller shared equity contributions help households further up the income spectrum, who are likely to be closer to home ownership but could get there faster with shared equity assistance (representing a smaller cost to the Crown per household);

*Noted*

- c **Note** that larger shared equity contributions reach further down the income spectrum, but represent a higher cost to the Crown on a per household basis;

*Noted*

d

s 9(2)(f)(iv)

e

- f **Indicate** whether the Government's proposed shared equity scheme to support KiwiBuild should focus on assisting:

- i. households on the cusp of being able to afford a KiwiBuild home who do not need significant financial assistance and therefore a lower amount of Crown equity (option 1);

*Yes / No*

- ii. lower income households likely to need significant financial assistance and therefore a higher amount of Crown equity (options 2 and 3);

*Yes / No*



- g **Note** our initial view is that the scheme is unlikely to be an attractive proposition to private sector investors, without enhancement that undermines the objective of the scheme or the value proposition for the Crown;

*Noted*

- h **Direct** officials to prepare a bid for Budget 2019 to establish a government funded and administered shared equity scheme to assist first home buyers to purchase KiwiBuild homes;

*Yes / No*

- i **Note** that if the Government decides to pursue a bid for a government funded and administered shared-equity scheme in Budget 2019, we recommend substituting the broad procurement process to identify private sector investment in a range of housing tenures proposed in our previous advice [0642 18-19] for a more targeted approach and deferring the bid for a tagged contingency to support this until Budget 2020;

*Noted*

- j **Agree** to defer the bid for a tagged contingency to support a targeted procurement process to identify private sector investment in the housing continuum until Budget 2020;

*Agree / Disagree*

- k **Note** that, subject to your decisions on this briefing, we will prepare further advice in the coming weeks to support the budget bid, including design of the scheme, eligibility and prioritisation criteria, and associated administrative processes.

*Noted*



Hilary Eade  
**Manager, Housing System Performance**  
**Housing and Urban Branch, MBIE**

Hon Phil Twyford  
**Minister of Housing and Urban**  
**Development**

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Hon Jenny Salesa  
**Associate Minister of Housing and**  
**Urban Development**

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## Background

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10. On 6 September 2018, officials from MBIE and MSD met with you to discuss advice [0642 18-19] about how government might support:
  - progressive home-ownership schemes to support the sale of KiwiBuild homes, both to households on the cusp of home ownership and further down the income spectrum
  - more new build rental housing (public, sub-market and market) to provide secure, good quality and affordable housing for households likely to remain in the rental market.
11. Our advice was informed by market soundings with a range of potential providers and investors. It explored ways to mobilise private sources of capital into progressive home ownership schemes, rather than direct government funding and provision. We identified that private and institutional investors would seek a risk adjusted return commensurate with returns on other investments (eg. commercial property, returning around 7%).
12. In summary, our advice proposed:
  - A procurement process, beginning with a Registration of Interest (ROI), to identify commercial opportunities and the level of government contribution necessary to attract private sector investment into progressive home ownership schemes (as well as other housing for the 'missing middle' generally eg. build-to-rent). We proposed revisiting direct government provision of progressive home-ownership schemes if the ROI failed to identify attractive commercial opportunities.
  - Developing a budget bid for an Affordable Housing Fund to provide outcomes-based funding to enable not-for-profits to assist those on lower incomes into public housing, affordable rental housing and home ownership. This would enable existing providers to scale up existing progressive home ownership schemes tailored to different household circumstances (eg. rent-to-buy) and leverage philanthropic capital.

## Your feedback

13. You asked officials to develop further advice on an option to establish a Government funded and administered shared equity scheme to support the sale of KiwiBuild homes, including a potential bid for Budget 2019. You indicated an interest in exploring how such a scheme could attract private investment over the longer term, including from iwi and institutional investors.
14. You expressed a preference that the Affordable Housing Fund support the growth of a small number of larger organisations rather than many smaller ones. You asked that officials reconsider access to the fund for local authorities to add new supply to their housing portfolios. We will report back to you with further advice on the proposed Affordable Housing Fund in October 2018.

## Ministerial Advisory Group feedback

15. On 14 September 2018, we provided the Ministerial Advisory Group (MAG) with copies of our advice and discussed our proposals with them. The MAG expressed support for the proposed Affordable Housing Fund and mixed tenure developments such as the Waimahia Inlet development.<sup>3</sup> We understand the MAG intends to provide you with separate advice about their discussions.

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<sup>3</sup> This development includes market sales and rentals, and CHPs offering sub-market rentals and progressive home ownership to low income households, as well as public housing. It is being led by a



## Policy objective

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16. We understand your objectives are to ensure the success of KiwiBuild to increase home ownership and improve housing affordability by:
- ensuring KiwiBuild homes are sold in a timely manner, allowing the government's capital investment to be recycled to enable the building of further KiwiBuild homes
  - assisting first home buyers to purchase KiwiBuild homes who would otherwise be unable to afford them
  - ensuring any assistance offered to first home buyers to purchase KiwiBuild homes is cost-effective for the Crown, including leveraging private sector investment where this represents value for money.
17. We have analysed the options in this paper against these objectives, with different options achieving these objectives to varying degrees.

## Problem definition

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18. Despite the KiwiBuild price caps and current government home ownership assistance, many renting households are unable to afford KiwiBuild homes due to insufficient income to service a mortgage and/or deposit. This raises the risk of there being insufficient first home buyers willing, eligible and able to purchase KiwiBuild homes when the programme reaches peak production in 2020/21.

## A shared equity scheme to support KiwiBuild

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19. The August market soundings undertaken by MBIE identified that shared equity and shared ownership schemes work best for moderate income households who already have a reasonable deposit, but who cannot afford to service a mortgage on the full balance of the house's value.
20. A shared equity scheme is a good fit for those on the cusp of being able to afford to service a mortgage on a KiwiBuild home (households just above the median income, eg. income decile 6), but is unlikely to be suitable for households further down the income spectrum (eg. income decile 5). Lower income households would be better served by a broader range of progressive home ownership schemes and tailored support services, such as those offered by existing community housing providers (CHPs). Such households would be supported by our complementary proposal for an Affordable Housing Fund.<sup>4</sup>
21. For a government-backed shared equity scheme, our working assumption is the government's equity share would be secured by a shared equity mortgage. The government's share would be repaid over time as the household's income rises and they become able to sustain larger mortgage repayments.<sup>5</sup> The occupier would increase their primary mortgage borrowing and use the funds to buy out the Government's share over time, eventually transitioning to full ownership. The Government's equity share could also be repaid if the occupier chooses to sell the house.

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partnership comprising the Tamaki Collective, New Zealand Housing Foundation, Community of Refuge Trust, Te Tumu Kāinga, Accessible Properties, Habitat for Humanity and Monte Cecilia Housing Trust.

<sup>4</sup> We note the goal in the Confidence and Supply Agreement between Labour and the Green Party to "Deliver innovative home ownership models within the State and broader community housing programme" and that a "Rent to Own scheme or similar progressive ownership models will be developed as part of Labour's KiwiBuild programme."

<sup>5</sup> As the occupier started out without enough income to sustain full ownership, this means their income would likely need to rise over time in order to achieve full ownership.

## Critical issues for further analysis

22. To progress a budget bid for consideration in Budget 2019, we need to clarify your objectives for the scheme and identify possible funding parameters upon which costs can be modelled. How we design and target the scheme would have significant implications for the overall cost and for the number of households assisted.
23. This paper seeks your feedback on the following critical issues:
- **Who to target** – targeting those on the cusp of affordability or further down the income spectrum.
  - **How much assistance/equity to offer** – this will have implications for how far down the income spectrum the scheme is able to reach.
  - **Eligibility requirements** – eligibility criteria for those participating in the scheme; for example, income and asset caps.
  - **Mobilising private sector investment** – the feasibility of this if the Government were to sell off its shared equity portfolio.
24. After analysing each issue we have included a box of text with some points we would like to discuss with you.

## Who to target and how much assistance to offer?

*The more equity the Crown contributes per household, the further down the income spectrum the scheme reaches...*

25. Smaller shared equity contributions help households further up the income spectrum, who are likely to be closer to home ownership but could get there faster with shared equity assistance. This represents a smaller cost to the Crown per household. Larger shared equity contributions reach further down the income spectrum, but represent a higher cost to the Crown on a per household basis.
26. We have analysed the implications of these two different approaches to help decide how much assistance the scheme should offer depending on whether your objective is to:
- assist as many households into KiwiBuild homes as possible by targeting those on the cusp of being able to afford a KiwiBuild home and who therefore do not need significant additional help
  - assist low to medium income households (eg. below the cusp) to purchase KiwiBuild homes who are likely to need significant equity and may need additional support services (eg. tailored financial literacy support).
27. Table 1 compares the advantages, disadvantages and cost implications of pursuing these two different objectives.

### *Māori and Pacific households*

28. Māori and Pacific households are represented in both groups set out in Table 1. Households with incomes in deciles 6-8 are on the borderline of KiwiBuild affordability,<sup>7</sup> and Māori and Pacific households are evenly represented in these deciles, suggesting a scheme targeted at those on the cusp of KiwiBuild affordability may effectively assist these households to service debt.
29. A scheme that reaches further down the income spectrum would assist further Māori and Pacific households, as these groups are increasingly overrepresented down the income spectrum (refer Annex Two for a graph showing distribution of individuals by ethnicity across individual income deciles).
30. Māori and Pacific households have a lower median net worth than European households, suggesting existing Crown products, such as the Welcome Home Loan may be particularly needed for these households have an adequate deposit.

<sup>6</sup> In particular, the two priorities for "Lifting Māori and Pacific incomes, skills and opportunities" and "Reducing child poverty and improving child wellbeing, including addressing family violence".

<sup>7</sup> Household incomes of \$80,200 to \$142,799 and individual incomes of \$34,400 to \$68,199.











### Mobilising private sector investment

47. In the short term, we understand your primary objective is to establish a government funded and administered scheme. However, in the longer term, you have also signalled an objective to explore the possibility of attracting private sector capital into such a scheme. One scenario would be for the Crown to sell its portfolio of shared equity portions to private sector investors. This would free up the Crown's investment for spending on other government priorities. However, private sector investors are only likely to be interested if the shared equity portfolio offers an attractive risk-adjusted return.
48. There are various ways a shared equity scheme could be structured to provide a return to private sector investors:
  - require the household to pay a rent or interest on the portion of the house they occupy but do not own. This would have the added benefit of incentivising the household to pay back the shared equity portion faster.
  - private sector investors receive any capital gains on the shared equity portfolio. However, our market soundings indicated institutional investors are not interested in speculating on capital gains. Their return could be enhanced by providing a disproportionate share of the capital gains on the property (eg. taking the capital gain on the whole house), or providing a government subsidy or underwrite on the expected capital gain returns (our market soundings indicated investors would seek a risk adjusted return commensurate with returns on commercial property).
49. Each of these approaches has disadvantages, as set out in Table 3.

<sup>12</sup> *Shared ownership* - the non-occupant's (eg the Crown's) property interest is secured through co-ownership. *Shared equity* - the non-occupant's (eg the Crown's) property interest is secured by a shared equity mortgage. A shared equity mortgage is technically a debt product, under which the non-occupant mortgagee (eg the Crown) receives a share of any capital gains in lieu of interest.

50. Our initial view is that the scheme is unlikely to be an attractive proposition to private sector investors, without enhancement that undermines the objective of the scheme or the value proposition for the Crown. We propose to revisit this once further details of the scheme are developed.

## **Risks and potential mitigations**

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51. Table 4 sets out the key risks and mitigations identified for the shared equity scheme proposed in this paper (ordered by short term to long term risks).

### **Implications for proposed procurement process to mobilise private sector investment and potential budget bid for tagged contingency**

52. In our initial advice [0642 18-19], we proposed that officials prepare a procurement process (beginning with a ROI) to gather further information about commercial and semi-commercial options to facilitate new build rental housing (public, sub-market and market) and progressive home ownership schemes. We also proposed seeking a tagged contingency in Budget 2019, to demonstrate the Crown's commitment to this process and so that any compelling proposals could be rapidly progressed without having to wait for Budget 2020. This ROI was intended, among other things, to flush out opportunities to support private sector administered shared equity schemes.



## Other ways to support the sale of KiwiBuild homes and increase progressive home ownership schemes

55. A government funded shared equity scheme is one way to mitigate the risk of there being insufficient first home buyers willing, eligible and able to purchase KiwiBuild homes once the programme ramps up. Table 5 provides initial analyses for two other options and compares them to the proposed shared equity scheme:
- offer first home buyers a deposit subsidy (beyond that already offered by HomeStart grant)
  - offer unsold KiwiBuild homes to institutional investors to seed the build to rent market.

**Table 5: Analysis of additional options to support sale of KiwiBuild homes**

Option	Advantages	Disadvantages
Government funded and administered shared equity scheme to support sale of KiwiBuild houses	<ul style="list-style-type: none"> <li>• Supports sale of KiwiBuild homes</li> <li>• Opens up KiwiBuild affordability to more households</li> <li>• Government's equity share can be recycled as households pay it back</li> </ul>	<ul style="list-style-type: none"> <li>• Significant cost to the Crown</li> <li>• High administrative overhead</li> <li>• Helps those at or near the cusp of home ownership rather than targeting funding to those with the most immediate housing needs</li> </ul>
Deposit subsidy (beyond that already offered by HomeStart grant)	<ul style="list-style-type: none"> <li>• Supports sale of KiwiBuild homes</li> <li>• Opens up KiwiBuild affordability to more households</li> <li>• Low administrative overhead compared to a shared equity scheme</li> </ul>	<ul style="list-style-type: none"> <li>• Government's investment is not paid back</li> <li>• Helps those at or near the cusp of home ownership rather than targeting funding to those with the most immediate housing needs</li> </ul>
Offer unsold KiwiBuild houses to institutional investors to seed the build to rent market	<ul style="list-style-type: none"> <li>• Increases the supply of market rental housing</li> <li>• Addresses rental affordability issues</li> <li>• Supports security of tenure and rental quality objectives</li> </ul>	<ul style="list-style-type: none"> <li>• Deviates from the KiwiBuild first home buyer objective (does not add to the pool of first home buyers able to afford a KiwiBuild home)</li> <li>• May be less attractive for KiwiBuild's development partners (who may prefer owner occupiers instead of renters)</li> </ul>

56. Similarly, there are ways to increase the delivery of progressive home ownership schemes other than by direct government funding, as canvassed in our previous advice and proposals for an Affordable Housing Fund and procurement process to gauge private sector investment in housing (particularly build to rent and community housing) [refer 0642 18-19]. Not all of these options are mutually exclusive and some work would best as complementary interventions.

### *For discussion*

57. Your feedback is sought on whether you would like further advice on any of the above options before deciding to progress a budget bid for a Government backed shared equity scheme.

58. Our recommendation is to prioritise the Affordable Housing Fund bid, as it aligns with the 2019 Wellbeing Budget priorities and represents value for money by leveraging private and philanthropic funding into public good housing outcomes. However, this scheme could be complemented by a government backed shared equity scheme aimed at those on the cusp of being able to afford a KiwiBuild home.

## **Next steps**

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59. Subject to your decisions on this briefing, we will prepare a bid for Budget 2019 to establish a government funded and administered shared equity scheme to assist first home buyers to purchase KiwiBuild homes. We will commence work on the detailed design of the scheme, including designing eligibility and prioritisation criteria, the product itself (or negotiating the rights to use an existing product), and the associated administrative processes. If the budget bid is approved, we would prepare a corresponding business case, for Cabinet approval (as per the requirements of Cabinet Office Circular CO (15) 5).
60. We will report back to you with further advice on the proposed Affordable Housing Fund in October 2018. We will provide you with further advice on a review of the current Crown home ownership products in March 2019.

## **Annexes**

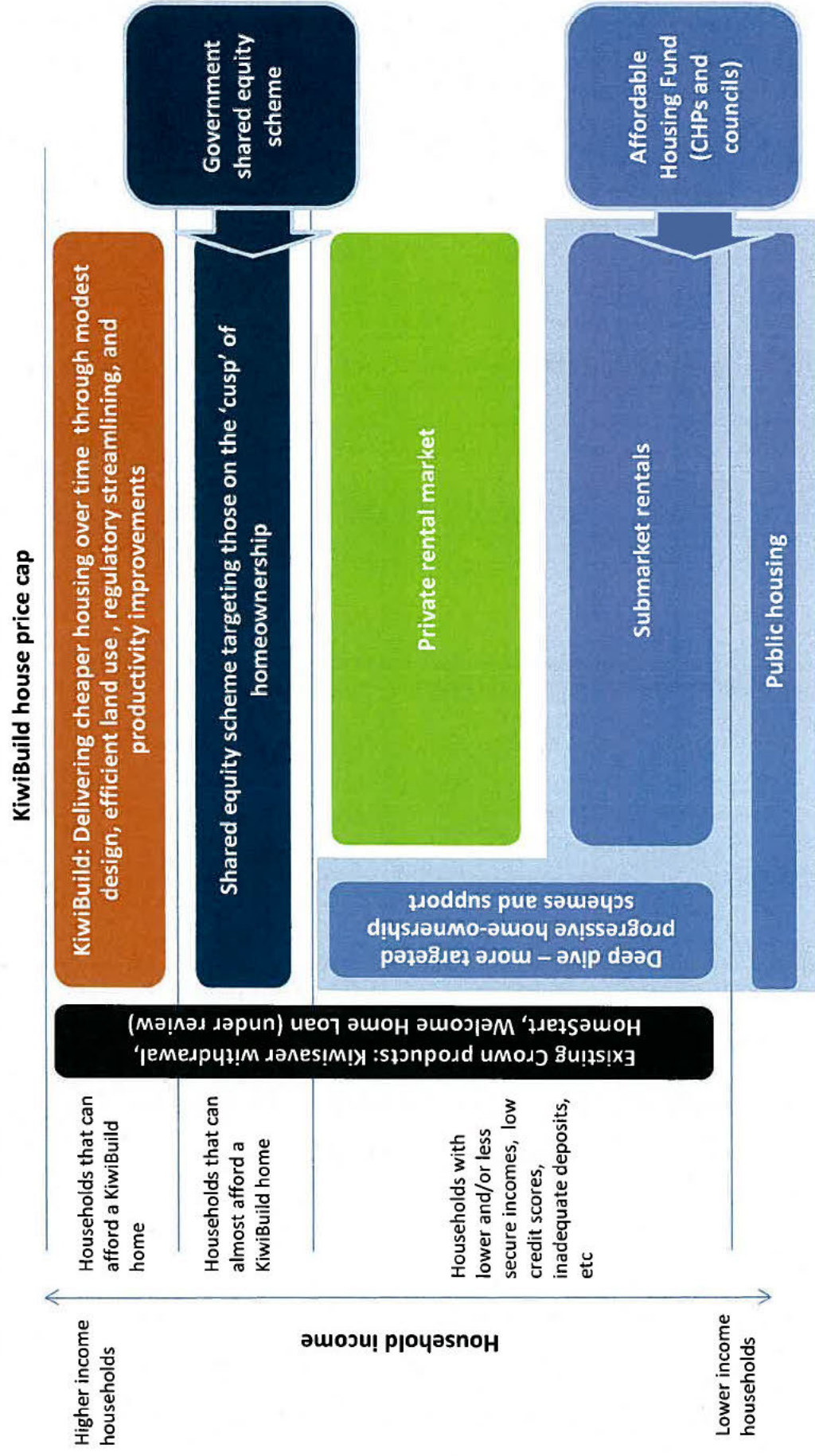
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Annex One: Diagram showing market segmentation of different proposals

Annex Two: Modelling the cost of different shared equity options



## Annex One: Diagram showing market segmentation of different proposals







### Household income deciles

Annual household income deciles									
1	2	3	4	5	6	7	8	9	10
Under \$23,900	\$23,900 to \$36,499	\$36,500 to \$49,399	\$49,400 to \$64,399	\$64,400 to \$80,199	\$80,200 to \$97,599	\$97,600 to \$117,699	\$117,700 to \$142,799	\$142,800 to \$188,899	\$188,900 +

Source: Household income and housing-cost statistics: Year ended June 2017, Stats NZ.

### Māori and Pacific households

62. Note the table above shows annual household income, whereas the graph below shows individual income.

### Distribution of individuals by ethnicity across personal income deciles



\*Source: 2017 Household Economic Survey