Summary of Sustainable Financing of Housing Public Hearings November 2012

For an Equitable Sharing of National Revenue

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1. Introduction

Despite impressive progress since 1994 – delivering nearly three million fully subsidised houses to low-income households – South Africa still has an unmet demand of over two million houses, which is rising. The cost of meeting this demand is far beyond the state's current fiscal capacity, especially given the global financial crisis. An urgent paradigm is needed to address the country's housing shortage. The Financial and Fiscal Commission (the Commission) embarked in 2011 on a public hearing process, aimed at making a novel contribution to the current debate on human settlements and financing of housing. A broad range of stakeholders are involved, including the three spheres of government, housing finance institutions, developers and NGOs.

The latest phase was the second set of public hearings on Sustainable Financing of Housing, which took place on 8–9 November 2012 at the Protea Hotel Waterfront, Centurion, Tshwane, Gauteng Province. As a basis for discussions at the public hearing, the Commission's research team, working with Shisaka Development Management Services (Pty) Ltd (Sishaka), developed and released an analysis of options for addressing housing finance and delivery challenges.

This Options Analysis was based on a problem statement, which had been validated by stakeholders at the previous public hearings in October 2011[1]. Prior to the actual work on the analysis and development of report, the Commission had consulted one-on-one with a wide range of stakeholders, some of whom gave presentations in response to the Options Analysis in November 2012. These consultations are on-going.

Summary of process

October 2011	First round of public hearings on sustainable financing of housing. The focus was on analysing the problems and challenges (not solutions). Stakeholders made extensive submissions and inputs that were incorporated into a problem statement.
February 2012	Publication of the formal problem statement.
Jan–Oct 2012	Commission's research team and Shisaka developed an analysis of options for addressing housing finance and delivery challenges. The Commission consulted one-on-one with a wide range of stakeholders.
November 2012	Second round of public hearings on sustainable financing of housing at which the Commission presented the options, and various stakeholders gave presentation in response to the Options Analysis.

The Options Analysis report presented by the Commission examined alternative paradigms for housing delivery, based on identified problems. The report reviewed the long-term consequences and implications of the current housing delivery and funding system, explored ways of encouraging the leveraging of household savings and looked at alternative roles and responsibilities for government and the private sector. Housing finance alternatives were developed using a financial model that looked at the resources required (including cost, funding and land).

The intention of the report and options presented was not to formulate a specific housing strategy but to identify various supply-side, demand-side and investment interventions and to evaluate the fiscal, economic and household impact of different options applied to alternative housing circumstances. All this has been undertaken in order to stimulate debate on how best housing finance should be reviewed.

[1] A summarised problem statement is available on FFC website

This document is a summary of some of the key themes that emerged from submissions and group discussions of the 67 stakeholders represented at the second public hearing. It is important to note that, at the moment, this report does not represent views of the Commission but includes consolidated views on the options presented and the outcomes of breakaway groups that examined housing circumstances. In order to facilitate and focus group discussion, three groups were established, with each group focusing on one of the following housing circumstances:
(1) Formal owned and formal rental housing;
(2) Informal settlements housing;
(3) Backyard and traditional dwelling housing.

Each housing circumstance was examined within the context of the constitutional right of access to adequate housing on a progressive basis. The groups discussed how the current supply-side, demand-side and investment interventions might be improved and explored the role of the state, the private sector and households.

The Commission will in due course release a more comprehensive document outlining in greater detail stakeholder perspectives articulated at the hearings, as well as its own recommendations.

2. Housing finance context

Stakeholders acknowledged the importance of the state's support to housing and the progress made – since 1994 nearly three million fully-subsidised houses have been built. However, despite a significant increase in the budget allocated to housing, the unmet demand is rising, and today more than two million households are presumed to have inadequate access to housing. The stakeholders agreed that the current housing finance policy is unsustainable. Increased costs over time mean that more and bigger subsidies are required to deliver on commitments. The budgetary implication of eliminating the housing backlog is estimated at R35 billion, which is far beyond the fiscal capacity of the state, especially within the context of slower economic growth.

In view of the current macro-economic situation and fiscal constraint, stakeholders recognised the need to look at how state support can be refined and resources better utilised. To realise the goal of adequate housing for all, some of the interventions that have been identified include the following:

- Supply incentives, which stimulate the supply of housing and imply that the state trusts the market (private sector);
- Demand incentives, which enhance the effective demand for housing by improving affordability (for example, through housing vouchers); and
- Investment incentives, which entail broadening the suppliers to include large-scale companies and households.

The starting point is to understand (1) the housing demand, which is a function of the demographic profile, location, tenure and price, and (2) the housing supply, which is a function of land, finance, infrastructure, regulation and construction.

3. The Model

The Commission, working with Shisaka, developed a financial model that was used to cost selected housing funding alternatives. Demographic data was taken primarily from the 2007 Community Survey, as the 2011 Census data was not available prior to the public hearing. The financial parameters used in the model were from publicly available information about subsidies,

mortgages, insurance, and housing supply and demand, while the cost data for developing land infrastructure and housing was based on previous work and input from sector experts.
The model followed a basic logical framework in which households housing circumstances were first identified. These were:

- formal – owned;
- formal – rented (plus room not in backyard);
- informal settlement (owned and rented);
- backyard dwelling (owned and rented);
- traditional dwelling (owned and rented);
- hostel; and
- other.

The circumstances were matched to a set of supply-side, demand-side and investment interventions and then assessed according to certain criteria, as explained below. The supply-side interventions modelled per circumstance were divided into: informal settlement interventions, backyard rental, new family formation and housing ladder, formal owned and rented, and traditional dwellings. The demand-side interventions modelled were incremental housing intervention (for example housing vouchers) and bonded housing market (for example mortgage tax deduction or Finance-Linked Individual Subsidy Programme[2] (FLISP) adjusted). Finally, the investment interventions applied only to privately developed residential rental and household rental up to an income level above R20,000.

The model looked at the total unit price of the housing product by intervention. Just over 34 interventions were analysed and applied to relevant housing circumstances. These interventions were compressed into four scenarios to obtain an understanding of how the different interventions could be combined and applied to the current housing circumstances.

The four scenarios[3] were:

1. Historic practice, which covers the provision of subsidy-linked housing units (large and medium-scale RDP housing projects), social housing, rental stock, lower-end mortgage financed housing with a FLISP subsidy.
2. Lowest cost to the state, which modelled interventions within each housing circumstance that have the lowest cost to the state.
3. Formalisation of informality, based on Outcome 8, concerning the in-situ upgrade of informal settlements and the formalisation of informal structures in backyards of existing formal houses.
4. National Development Plan, with a focus on creating more compact, dense, efficient and equitable cities, developing infill land parcels and redeveloping/converting inner city areas.

The assessment criteria were:

- Overall impact on household, which was determined as a product of entitlement to access subsidies, affordability applying applicable financial terms, and creditworthiness.
- Contribution towards integrated, inclusive and equitable cities, based on the extent to which the intervention is not implemented on the periphery of the city and to which it contributes towards densification (< than 40 units per hectare).

[2] FLISP, or the Finance-Linked Individual Subsidy Programme, is a housing subsidy launched in early 2012 for households earning between R3,501–R15,000 who are buying a house worth R300,000 or less.
[3] For analytical purposes, four scenarios were chosen. However, the model is much more flexible.

- Impact on market distortions, which included impact on competition, risk allocation, transparency and transaction cost/duplication.
- Contribution to an effective housing market, based on the amount of gearing secured by the non-state sector.

Stakeholders agreed that the model showed a combination of supply, demand and investment incentives to be more efficient. Supply-side options that mobilise households and private firm responsibility seem effective, and demand-supply interventions show promise (for example, housing vouchers). Stakeholders pointed out that the model needs to be extended, to capture broader benefits beyond just the household, to include ‘renting to buy’ as an option and to look at rural housing in more depth.

4. Participation of all players

Stakeholders agreed on two principles: (1) housing interventions should respond to the housing situation and household affordability, and (2) the housing system should maximise the participation of all players (state, private sector and households). The housing system needs to move away from the current situation whereby state offers subsidies (in the form of RDP housing and the FLISP) to encourage greater participation by households and the private sector. The state’s contribution has to be the smallest, and government resources should be used to leverage massive private sector investment.

Stakeholders proposed that the role of the state is to provide certainty through secure tenure and land regulation, to invest in public infrastructure, and to encourage household investment in housing. Instead of incentives that encourage households to wait (in a queue for state-provided housing), the state should explore incentives for households to invest in their own housing. State incentives should be designed to respond to the heterogeneity of the housing market and to assist communities and individuals to assess finance. The cost of state land holdings and improving procurement processes also need to be looked at.

5. Formal owned and formal rental houses

This housing circumstance covers bought (owned), rented (temporary ownership) and free (own) houses that provide protection from the elements, space, health and safety, links to economic and social facilities, and tenure. This market segment needs more transitional low-cost rental housing and rent-to-buy options.

Stakeholders felt that any intervention in this segment should maximise the participation of all players – the state, households and private sector. The paradigm of what the state is expected to deliver needs to shift. The state should be encouraging citizens to contribute to the cost of their housing, limiting the entitlement to free housing to the very poorest. For formally owned houses, the state should provide services, such as electricity, water and sanitation where backlogs exist, while the households should build the top structure. To help poorer households, stakeholders suggested that the state provide vouchers, which households could use to purchase building material. The household’s contribution would depend on household income: the higher the cost, the more the household should contribute. Stakeholders proposed that households should be encouraged to save towards meeting their housing needs, through for example a savings scheme similar to Fundisa[4]. Private sector involvement in this market could be stimulated by the state

[4] Fundisa is a unique savings product and an industry initiative between the Association of Savings and Investment South Africa (ASISA), the government and various financial institutions. It aims to assist learners to

ensuring the social infrastructure is upgraded (to support efficient land use) and managing the bureaucracy. This would provide assurance for the private sector to build houses and increase access from temporary ownership (rental) to permanent ownership.

6. Informal settlements

In the case of informal settlements, stakeholders agreed that the services provided to the location and the shelter must be separated. Stakeholders felt that responsibility should be devolved to the community level and in-situ upgrade of the settlements should be covered by a differentiated policy based on different needs. For this to happen, the state must capacitate civil society and enter into dialogue with communities to determine their needs. The other responsibilities of the state include providing tenure protection, access to social and economic infrastructure, (e.g. schools, clinics, public transport and roads), and technical support and incentives (for example cheap material for building homes).

Stakeholders suggested that current interventions could be improved by consolidating supply-side subsidies and fast-tracking the implementation of the Inclusionary Housing Policy. Other areas that need addressing include developing a proper rural development plan and fast-tracking processes of establishing townships. Mechanisms should be introduced to address the capacity and skills at provincial level, the flow of funding and the supply of land. Stakeholders agreed that the expectations of households must be managed, while the option of backyard/cheap rental should be promoted for those inhabitants who do not qualify for assistance and do not have families.

7. Backyard dwellings and traditional dwellings

Stakeholders felt that backyard dwellings should meet minimum standards, which will require standardising and streamlining the sometimes cumbersome municipal regulations. Such dwellings should consist of a formal structure and have access to basic infrastructure such as sanitation, water and electricity. Municipalities need to review existing by-laws and survey people living in backyard dwellings. Stakeholders were of the view that some useful lessons will emerge from the Gauteng backyard policy/subsidy to owner initiative, which incentivises owners to upgrade their dwellings. Currently no supply-side, demand-side or investment interventions exist for backyard dwellings.

Like for backyard dwellings, minimum standards should also exist for traditional dwellings, which should be on stands large enough to allow for traditional activities such as gardening. To ensure cost-effective provision of basic infrastructure (such as sanitation, water and electricity), settlement planning should be done in consultation with traditional leaders.

Stakeholders noted that in the case of these types of dwellings, progressive realisation is when the state provides basic services (and later improvements when additional resources are available), and the households then progressively improves on what has been provided. The state should provide basic infrastructure, planning services, and assist poor households to access housing. The households need to take responsibility for meeting their housing needs instead of expecting the state to provide everything. Landlords (in the case of backyard dwellings) and households

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further their studies at a tertiary level. The Fundisa Fund is a unit trust fund that focuses on savings for education. Investors in a Fundisa Fund account receive an annual bonus equivalent to 25% of the money saved – to the maximum of R600 per year – that is added to the savings. This bonus is only to be used for tertiary education expenses.

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(traditional dwellings) should bear the highest cost, with grants available to people renting backyard dwellings. Some stakeholders pointed out that the interest rate could be reduced if government provided guarantees to the unsecured loans, which would also increase the amount of available loans.

8. Conclusion

It is clear that a change in the approach to housing finance will be the subject of on-going consultations. Stakeholders reflected a real desire to modify the framework while continuing to champion the Constitution’s housing objectives. Stakeholders recognised that the housing paradigm needs to shift, from one of entitlement to one of taking responsibility. Housing is the responsibility not only of government, but of all players including households and the private sector. Incentives are needed that will encourage the private sector and households to finance housing, as the state does not have enough resources to provide the number of houses on the scale required. The role of the state is to provide certainty, to use government resources to supply basic services and infrastructure, and to leverage private sector and household investment – for example, transitional, low-cost rental housing and rent-to-buy options in the formal owned and rental market.

Improving the cost, scale and form of housing delivery is necessary, and the model showed a combination of supply, demand and investment incentives is more efficient. However, a key issue that emerged was housing affordability, and the need for households to save in order to participate in the housing market. Stakeholders noted that the biggest constraint to saving is the current level of household indebtedness, which could be improved through some of the interventions identified. In addition, the processes that lead to household formation and development and how city-wide markets work need to be better understood.

The next step is to look at what would be the best set of recommendations in order to address housing finance and delivery challenges. The Commission will explore this further in the full workshop report, as well as in its future engagements with stakeholders. A draft technical report, with an initial set of recommendations and policy options, will be released for further consideration by stakeholders. Stakeholders will be able to raise concerns and question the recommendations put out by the Commission.