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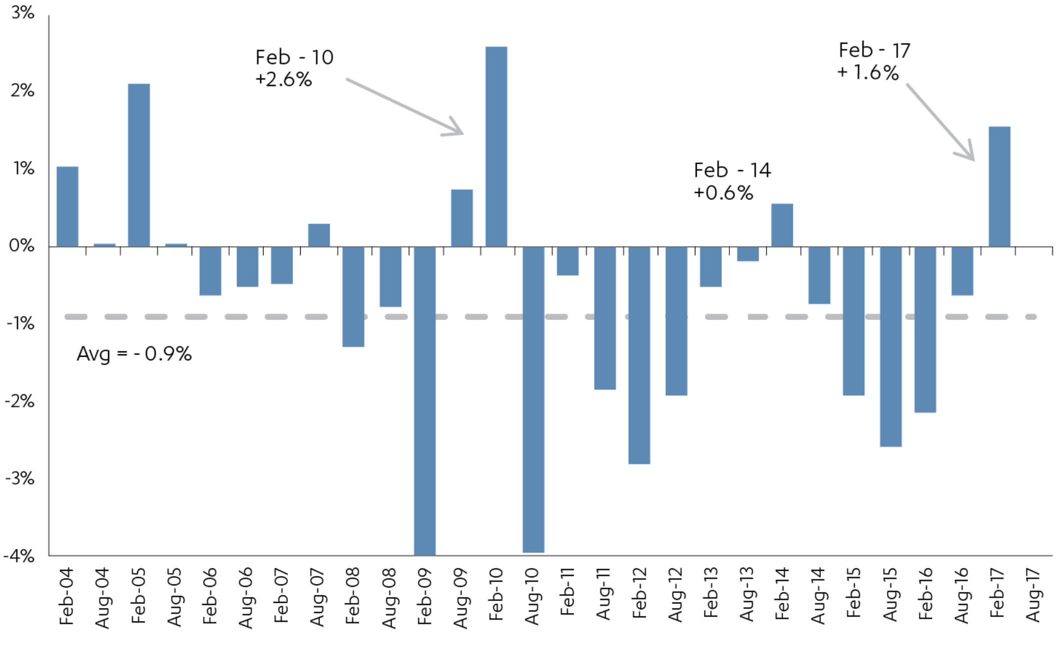
Reporting season gives reasons for optimism

Crispin Murray

At a headline level, the recent reporting season provided several reasons for optimism with Corporate Australia beginning to successfully adjust to the more subdued growth environment.

At first glance, the results do not deviate too far from historical norms: 22% of companies upgraded while 32% downgraded which, while better than last season, is broadly in line with the long-term average. More telling is the change in aggregate expected earnings for the S&P/ASX 200 in FY17, which increased by 1.6% as a result of reporting season. While this may not seem like much, as the following chart shows, it is the best result since February 2010 and stands in stark contrast to the average downgrade of -0.9% that follows reporting seasons.

S&P/ASX 200 EPS upgrades / downgrades for FY17



Source: Credit Suisse, Factset

The upshot is that the S&P/ASX200 remains on track for its first financial year of positive EPS growth since FY14, with upgraded expectations now at 16% growth for FY17, following -13% in FY16 and -3% in FY15. This is a remarkable turnaround, given the market expected 8% EPS growth for FY17 as recently as August 2016.

Resources resurgent

The caveat to all this positive momentum and earnings upside is that it was largely the result of a resurgent resource sector. Soft data at the end of 2015 saw the Chinese authorities administer an economic adrenaline shot via a credit injection and a renewed focus on infrastructure spending in early 2016. The result was an uptick in demand for resources which, in conjunction with supply disruption and discipline in iron ore and coal, have seen commodity prices soar. This, in turn, has seen a surge in cash flow and earnings for the miners, with their operational leverage enhanced by several lean years of cost cutting and, in some cases, near-death experiences. The turnaround has been spectacular, with cash flow funding debt reduction, dividends and buybacks, and share prices have surged accordingly.

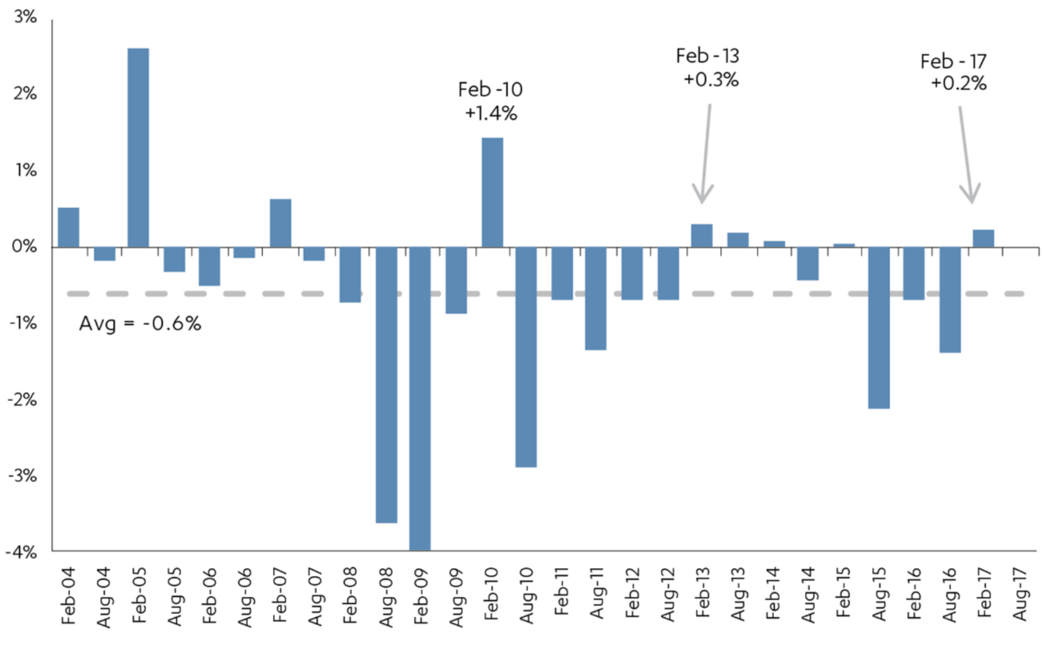
We would caution against excessive exuberance regarding the turnaround in earnings; it is not broad-based and, while resource companies have been adept in controlling costs and capex, it has been the exogenous factor of commodity prices which has driven their success.

Industrials less spectacular, but significant

Beneath the turnaround in resources there is something perhaps more surprising and potentially more significant: the market ex-resources (ie the industrials) did not, on the whole, disappoint.

The S&P/ASX 200, once commodity companies are removed, saw earnings expectations increase by +0.2%. Again, this does not seem much, but needs to be considered within the context of the average historical downgrade of -0.6% and the fact this is the best result since 2010.

S&P/ASX 200 ex commodities EPS upgrades / downgrades for FY17



Source: Credit Suisse, Factset

Cost discipline behind earnings upgrades

Earnings quality among the industrials was mixed. For all the nascent signs of optimism in this reporting season, we remain in an environment of muted revenue growth for most industries. Where companies beat expectations in this season, it was often a result of delivering surprisingly high levels of cost reduction.

Qantas provides a salient example. While it reported a 7.5% contraction in underlying pretax earnings due to the combination of softer domestic demand for much of 2016 and an increase in international industry capacity, the stock actually did well, as earnings were $25 million ahead of the market consensus. Cost discipline has allowed QAN's earnings to be more resilient than the market expected and enabled them to continue to return capital to shareholders.

Declining earnings quality drives underperformers

If cost discipline drove earnings upgrades and outperformance within industrials, any signs of declining cash flow or rising capital intensity drove the season's underperformers. There was an uptick in companies relying on a range of accounting measures in order to hit earnings targets, such as the inclusion of one-off profits, release of provisions, changes to depreciation and amortization policies, or changes in treatment of working capital. It is possible to discern, in the underperformance of previous market favourites who showed signs of deteriorating quality, a growing focus on cash flow, rather than accounting earnings.

This highlights the need for investors to go beyond headline reported earnings to understand the underlying profitability of the business. Ultimately, accounting earnings can be manipulated, to an extent. Cash flow cannot, and often offers a far more accurate gauge of a company's true health and fortune.

Look for strong strategy and ability to execute

All in all, Corporate Australia remains in reasonable health, underpinned by strong cost discipline. Management remained focused on capital management in preference to further capex and increased dividends and buy backs should serve to help support the equity market.

We remain mindful that we are in an environment of significant industrial disruption due to globalisation, developments in technology and changes in regulation. The combination of low revenue and industrial disruption sorts the wheat from the chaff in management quality. Only those companies with a strong strategy and the ability to execute will ultimately thrive. This is where we deploy our team and company-level insight to greatest effect, by finding the companies who are equipped to traverse today's challenging environment.

Crispin Murray is Head of Equities at [BT Investment Management](), a sponsor of Cuffelinks. This information is general only and does not take into account the personal circumstances or financial objectives of any reader.

Most housing affordability initiatives are a waste

Noel Whittaker

Housing affordability continues to dominate the headlines. And, as usual, there is no shortage of suggestions of how to make housing more affordable. Unfortunately, most of these ideas are impractical – implementation of any of them would simply increase the ability of first home buyers to buy a home and so increase demand. The only possible outcome of increasing demand is to push prices up even further, and continue the vicious cycle.

Think First Home Savers Grant, reduced stamp duty for first home buyers, and the ludicrous suggestion currently being debated that would allow first home buyers to access their superannuation for a house deposit.

Just last week we even had the governor of the Reserve Bank, Phillip Lowe, hinting that consideration should be given to reducing the capital gains 50% discount that is currently available for investors who have owned an asset for over a year.

My view on CGT changes

Capital gains tax (CGT) was introduced by the Hawke Keating government on 20 September 1985 as part of a general reform of the tax system. Prior to that, tax could be levied at full marginal rates on capital profits if the ATO decided that the owner's purpose when acquiring the asset was to re-sell it at a profit. This was a grey area, and many investors simply did not know what the taxation position would be on sale of an asset until the sale was completed and their tax returns were lodged. It was a nightmare.

There has long been general agreement that capital profits should be adjusted for inflation. This is why the Hawke Keating CGT legislation allowed investors to adjust the base cost for inflation before CGT was assessed.

But it was a different world then: interest rates were 14%, inflation 10%, and the top marginal tax rate was 60%, which cut in when income reached $35,001.

Given those numbers, it was quite a reasonable deal in 1985. The downside was that adjusting the base cost required onerous record keeping, especially with dividend reinvestment, requiring a separate cost base to be kept for each investment.

The Howard government simplified the system, effective from 20 September 1999: replacing the indexation method with what we have today – a 50% discount applying to assets held for more than 12 months.

Consider changing one year to five years

What is the logic behind calls to make housing more affordable by changing the 50% discount after 12 months? There is anecdotal evidence that some investors in Sydney are buying properties for a quick turnaround, and increasing the qualifying time for the discount may deter a few of them. But, given buying and selling expenses, you would need to make a hefty gross profit to make much real money, even with 50% off the CGT.

Being a long-time proponent of investing for the long haul, I have no problem with increasing the time that an asset may be held before the 50% discount is available. Even stretching the current one year to five years would not be unreasonable.

Faith in residential property would remain

But you are living in la-la land if you think that will make one iota of difference to housing affordability. The majority of investors in residential property are invested there because they are tired of the never-ending tinkering with the superannuation system, they do not trust shares, and they realise that money in the bank is never effective as a long-term investment. For them, residential property – usually held long-term – is the only way to go. Demand from these investors will continue until reasonable alternatives are available, which may be light years away.

Noel Whittaker is the author of Making Money Made Simple and numerous other books on personal finance. His advice is general in nature and readers should seek their own professional advice before making any financial decisions. Email: noel@noelwhittaker.com.au.

Reply from Chris Cuffe

The key premise of my article is that adjusting CGT for indexation is more equitable than a simple discount factor. It was not meant to say that if you do this one single measure, it will DEFINITELY cool the housing market. Housing affordability will need a range of policy issues, but it would be one less reason for investors to use tax as a motivation for buying property.

I repeat the quote in the article from a leading tax expert in Treasury:

"The concessionary treatment of capital gains income is arguably the primary motivation for financial investment in negatively geared real estate, which aims to shift all of the investment return into the capital gain on the eventual sale of the asset."

I would expect that if the CGT discount was changed to indexed gain AND negative gearing was restricted to the said property income (ie can't reduce other income) THEN there would be a material amount of heat taken out of the market.

Following my article, I was referred to some research called 'Mythbusting tax reform' by Deloitte, and its detailed analysis of the CGT concession. A table and a chart are worth highlighting.

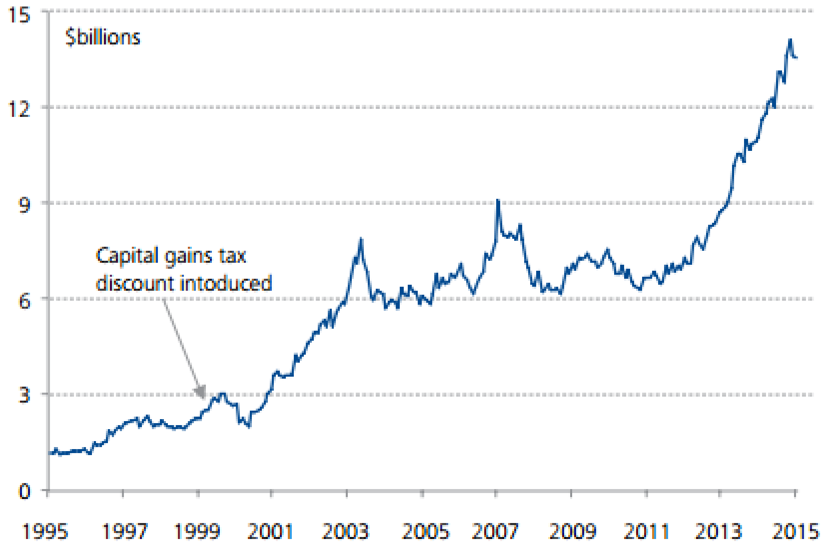
Table 1: CGT discount rates by type of taxpayer

Entity	Discount	Entity tax rate	Effective tax rate on capital gain
Complying superannuation fund	33 1/3%	15%	10%
Company	0%	30%	30%
Individual – at top marginal rate	50%	47% (MTR)[29]	23.5%
Individual – between $37k-$80K	50%	32.5% (MTR)	16.25%
Individual – between $18.2K – $37K	50%	19% (MTR)	9.5%

In the words of Deloitte: "Table 1 shows there are really big incentives for some taxpayers (such as high income earners) to earn capital gains, versus little incentive for others (such as companies)."

Chart 6 shows the rapid rise in investor activity in housing markets since the discount was introduced. Deloitte also shows that those earning more than $180,000 a year receive a larger share of net capital gains.

Chart 6: Investor activity in housing markets



Deloitte concludes on CGT: "The discounts Australia adopted back in 1999 assumed inflation would be higher than it has been – and so they've been too generous." Exactly my point.

If it's true, as Noel says, that changes to the tax treatment would not change investor demand, then at least the budget would be improved by increased tax collections.

I'm also not as convinced as Noel that investors are only interested in residential real estate, as if it had no competition from other investments. Flows into managed funds are massive at the moment, motivated by investors having a last grab at the higher superannuation caps before the 1 July changes. Products such as ETFs and LICs are experiencing strong growth. ETFs in Australia had inflows of $467 million in February 2017 alone, and there are three new LICs in the market hoping to raise a combined $1 billion. Additional boutique fund managers are still being launched every week, and share market investors have experienced excellent returns with lower volatility in recent years. I'm not doubting people are worried about global macro trends, but nevertheless, investors have driven the world's largest exchange to an all-time high.

Deductibility of contributions after 1 July is a big deal

Gemma Dale

With all the news about the superannuation changes for 1 July 2017 focussed on the negative impacts for investors, it's easy to lose sight of any possible opportunities.

While the changes have largely deleterious effects for those with very large balances or who are wishing to substantially increase their super balance through contributions, two changes will actually improve the opportunity for some to boost their savings.

Opportunity 1: Abolition of '10% test'

The first is the abolition of the '10% test'. Until 1 July 2017, a person must earn less than 10% of their income from eligible employment if they want to claim a personal tax deduction for a contribution to super.

A technical definition of 'total income' exists, which includes assessable income for tax purposes as well as reportable fringe benefits and reportable superannuation contributions to super (but not Superannuation Guarantee contributions, which are mandated). For the majority of people, this means that you can only claim a tax deduction for personal contributions if you are self-employed, or not earning a salary at all (ie, retired or unemployed).

If you're an employee, you may be able to salary sacrifice. If not, you are currently unable to claim a deduction for any personal contributions to super. This byzantine set of rules creates an uneven playing field.

While it appears a panacea for employees wishing to increase their super contributions, salary sacrifice arrangements can range from the advantageous to the seriously detrimental. Salary sacrifice is not a defined term under the law, and exists as an arrangement between an employer and an employee, with no requirements as to how that arrangement must be enacted. As a result, arrangements vary widely, and each individual needs to ensure that salary sacrificing through their employer is in their best interests.

Many employers offer no salary sacrifice arrangement, leaving an employee with no ability to make voluntary concessional contributions at all. Another employer could, for example, offer you the ability to reduce your salary through contributions to super, but then pay your mandated Superannuation Guarantee on the new lower amount. To illustrate, if you are earning $100,000 per annum, you would ordinarily receive an additional $9,500 per year in contributions to super (as per the current 9.5% Superannuation Guarantee rate).

If you have an unscrupulous employer, your decision to salary sacrifice $10,000 a year would reduce your salary to $90,000 per annum, and your SG payment to $8,550 (9.5% of the new $90,000 salary), a drop in super of $950 a year. An even more unscrupulous employer would cease paying your SG altogether, as the $10,000 per annum you are salary sacrificing technically meets the employer's obligation to pay 9.5% of your salary to super. This results in a $9,500 reduction in overall benefits. An employee who doesn't read the fine print could be severely disadvantaged without any recourse to their employer.

On the flip side, many employers offer generous matching arrangements through their salary sacrifice packages. This usually gives the employee a greater employer contribution if a sacrifice of some of the existing salary, for example, an extra 1% employer contribution for each 1% of salary sacrificed.

Employees are often left to determine the benefits of each or seek the assistance of a financial adviser who is familiar with the employer's scheme, if such an adviser exists.

One of the further challenges with salary sacrifice is that it requires long-term planning. All arrangements must be prospective in nature, and therefore windfalls and other lump sums are generally only contributed to super as non-concessional contributions if you're employed. *Some employers give the option to salary sacrifice a bonus on a prospective basis (i.e. before entitlement to it, but this is difficult to plan for without knowing how large the bonus will be).*

For many people the simple decision to have super contributions deducted from their salary on a fortnightly or monthly basis by their employer is an excellent method of forced saving. For others, it doesn't reflect the reality of variable income and expenses, and particularly unexpected cash flows from the sale of assets and other sources. For those with no ability to salary sacrifice, being unable to claim a tax deduction can reduce the incentive to contribute to super at all.

The abolition of the 10% test has the effect of doing away with all these challenges.

Individuals up to the age of 65 will be able to contribute to super and claim a deduction in their personal tax return; those between 65 and 75 will also be able to take advantage so long as they meet the work test to be able to contribute.

Salary sacrifice arrangements will continue where employers offer them. Employees can then consider whether salary sacrifice or personal contributions are more beneficial, or even consider a combination of both. A notice of intent must be submitted to claim a deduction for a contribution to a super fund, and timing issues need to be considered.

Opportunity 2: Five-year carry-forward rule

The carry-forward provision will give those with broken work histories, volatile income and other variable contribution patterns the ability to better utilise their concessional caps over a five-year period.

If you have total superannuation balances of less than $500,000, you will have the opportunity to utilise the unused portions of your concessional caps from previous years (up to five years' worth) in the following financial year, or future years. After five years, any unused amount will expire. The catch is that this change **will not come into effect until 1 July 2018,** so the first year to use a carried forward amount will be 2019-20.

This new rule benefits those who've been unable to use their concessional caps in full in prior years, such as agricultural producers with variable crop income, entertainers with periods of high and low income, and women who take time out of the workforce to have children.

The carry-forward contributions will be concessional, meaning you are claiming a personal tax deduction for them, and therefore you'll need to have sufficient assessable income to make that deduction worthwhile. As a result, this will largely benefit higher income earners, even if that high income occurs only one year in five.

For those with predictable periods of high income over several years, there may be benefits in planning concessional contributions for periods of higher income using carried-forward amounts in order to maximise the deduction. This change is a couple of years away giving time to plan.

Prior to these changes coming into effect, if the $1.6 million general transfer balance cap isn't likely to be an issue for you, consider using the current higher contribution caps while you are able.

Gemma Dale is Director, SMSF & Investor Behaviour at nabtrade, a sponsor of Cuffelinks. This information is general only and does not take into account the personal circumstances or financial objectives of any reader. Readers should seek independent advice before acting on any information.

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Portfolio diversification: when a free lunch can cause indigestion

Raewyn Williams

Diversifying investment portfolios is known to provide a rare 'free lunch' to investors. The value of diversification was demonstrated by Harry Markowitz, who also gave investment professionals one of their most beloved acronyms, 'MPT', when he established Modern Portfolio Theory in 1952. MPT demonstrates how diversification removes unrewarded risks in a portfolio without sacrificing return expectations.

Measuring risk factors

How effectively diversified a portfolio is can be measured a number of ways. Simple ways cover the number and variety of assets, managers, sectors and industries in the portfolio. More sophisticated measures capture how correlated the portfolio's assets are to each other (how closely their values move up and down together) and how much the performance of these assets can be explained by underlying common 'factor risks'.

Factor risks are attributes like size, value (for example, low price to book value), growth, momentum and volatility. A diversified portfolio spreads exposures across a range of factor risks, rather than loading up on one or two factor bets. Of course, an investor deliberately loading up on assets with particular-factor attributes (such as value stocks) is not necessarily being unwise. But the investor must recognise that this becomes more like a high-conviction, concentrated portfolio than a well-diversified one.

Portfolio diversification has benefitted investors since the advent of MPT, especially for large investors with billion-dollar portfolios at stake. However, there is a kind of 'indigestion' to this free lunch which we uncovered last year while analysing the Australian equity portfolio of one such large superannuation fund.

Superficially, the portfolio showed the qualities of a well-diversified equity portfolio, which was the objective of the fund:

- 11 discrete managers and styles
- 538 holdings of ASX-listed stocks
- a spread of between 20-88 ASX-listed stocks per manager
- exposures to five of the factor risks (size, value, growth, momentum and volatility).

Putting the jigsaw together

However, we discovered that this diversification was working against the fund in three critical areas.

First, it was hard for the fund to think about and analyse the portfolio as a whole. The complete picture could only be assembled by putting together the jigsaw of separately managed portfolio pieces. We did this by reconstructing the multi-manager portfolio in a centralised portfolio management (CPM) structure.

Second, we created a measure of 'portfolio redundancy', or the extent to which the 11 managers were holding very similar positions. We measured portfolio redundancy by calculating, per manager portfolio, the minimum of each stock's value held in both the specific manager's portfolio and the wider portfolio (ex-manager) – overlapping stock positions – and then summing these per-manager overlap figures on a weighted basis (reflecting manager weights within the total portfolio) as follows:

Equity Manager	Allocation	Total Names	Number of Unique Names	Overlap with Rest of Portfolio	Contribution
A	34.6%	49	5	52.2%	18.1%
B	18.7%	48	6	56.1%	10.5%
C	10.0%	88	21	51.2%	5.1%
D	9.8%	20	3	10.7%	1.1%
E	6.6%	44	0	51.5%	3.4%
F	4.4%	59	8	12.3%	0.5%
G	4.2%	38	4	9.2%	0.4%
H	3.5%	46	7	48.7%	1.7%
I	3.5%	32	8	3.6%	0.1%
J	2.6%	70	24	8.1%	0.2%
K	2.0%	44	0	53.9%	1.1%
				Portfolio Redundancy	**42.2%**

Too many similarities diminish diversification

Our portfolio redundancy calculation of 42.2% showed that the 11 managers were creating similar positions to each other over nearly half of the portfolio by value, or 452 of the total 538 stocks. Only 57.8% of the portfolio, across 86 stocks, was doing the heavy lifting to diversify the portfolio away from this common core.

This problem can arise in multi-manager portfolios which benchmark the underlying managers to similar indexes such as the S&P/ASX 300. 'Tracking error' to benchmark is a form of risk which these managers will not take on unless they expect to be rewarded. A large investor may think it is diversifying by spreading its portfolio over a number of managers, but if all the manager portfolios are tightly tracking a similar benchmark, there can be less diversification, and more portfolio redundancy, than the investor thinks.

Third, we classed each stock holding as a type of factor risk exposure to consider the level of factor risk diversification at the whole-of-portfolio level. Each of the 11 manager portfolios was expressed as a bundle of factor risks to detect how true to label each manager was (for example: was a value manager long the value factor? Was a defensive manager long the low volatility factor?). We identified two managers who were virtually identical to each other and another three who were very similar when profiled according to factor risks. Hence, three managers were adding nothing to the factor risk diversification of the portfolio.

False sense of security

This exercise shows how the free lunch of diversification can cause indigestion when it gives a false sense of security, complicating the portfolio and muddying the bigger picture, rather than reducing the risks of the portfolio.

There is another danger of using a wide suite of active managers with a seemingly diversified set of risks which can directly hit the investor's bottom line. If the collective risks, from a whole-of-portfolio perspective, look just like the market, then the investor is paying active management fees for a portfolio that could have been provided much more cheaply by an index manager or ETF provider.

Raewyn Williams is Managing Director of Research at Parametric Australia, a US-based investment advisor. This information is intended for wholesale use only and not for retail clients. Parametric is not a licensed tax agent or advisor in Australia and this does not represent tax advice. Additional information is available at www.parametricportfolio.com/au*.*

Australian ETF industry comes of age

Ilan Israelstam

The annual BetaShares/Investment Trends ETF Report provides a unique snapshot of the key statistics and drivers in the Australian Exchange Traded Fund (ETF) industry, from the perspective of individual investors, SMSFs and financial planners. This year's findings indicate a 'coming of age' in the Australian ETF industry.

Key findings of the Report

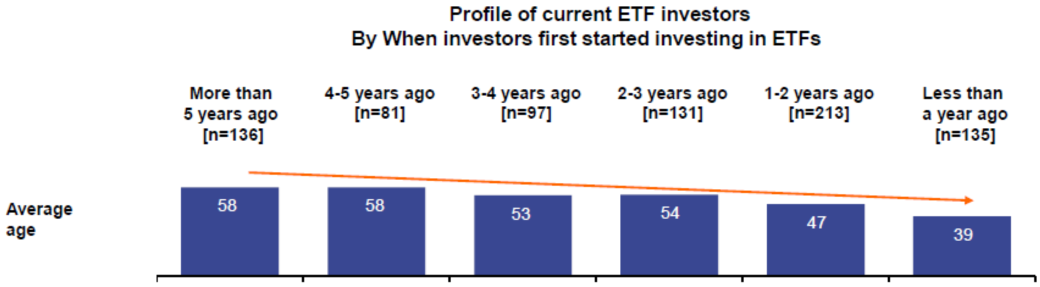
The insights gleaned from the research are based on responses from approximately 9,000 investors and 676 advisers, and include:

- The number of ETF investors in Australia grew at an annualised rate of 31% in the 12 months to September 2016
- Millennials are increasingly embracing ETFs; newer ETF users are significantly younger compared to 'early adopters'
- 38% of ETF investors invest via an SMSF with usage growing strongly
- Seven out of ten financial planners currently recommend ETFs or intend to do so in the future
- Advisers exhibit strong appetite for actively managed ETFs.

Size and growth: the emergence of the millennial investor

The number of Australian investors using ETFs has grown to a record number of 265,000, up from 202,000 in the previous year.

While ETF investors are on average 51 years old, including a third who are already retired, the average age of investors who invested in ETFs for the first time in the past year is 39 years, significantly lower than those who first started using ETFs five years ago at an average age of 58. This is a rather striking statistic and shows how mainstream the ETF industry in Australia is becoming, as well as how important the younger or millennial investor will be to the industry in the future.



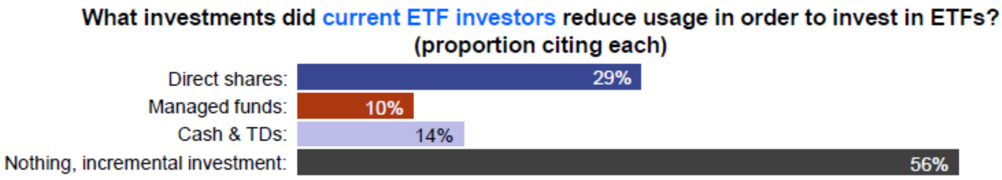
Source: BetaShares/Investment Trends ETF Report

To further emphasise this, among the online share investor population, the appetite for ETFs is greater among the younger cohort. About 37% of millennials say they use or intend to use ETFs in the coming year, versus 31% for Gen X investors and 28% for baby boomers.

Strong demand from retail and SMSF investors

Repeat investment into ETFs is high, with 70% of investors indicating they would consider re-investing in ETFs in the next 12 months.

The majority of investments into ETFs represents new money into the industry, with 56% of ETF investors buying the products with incremental investment monies, rather than decreasing their allocation to direct shares or managed funds.



Source: BetaShares/Investment Trends ETF Report

The number of SMSFs holding ETFs has grown in line with the increase in the number of ETF users, with 38% of ETF investors holding ETFs through their SMSFs. This investor class continues to drive industry growth.

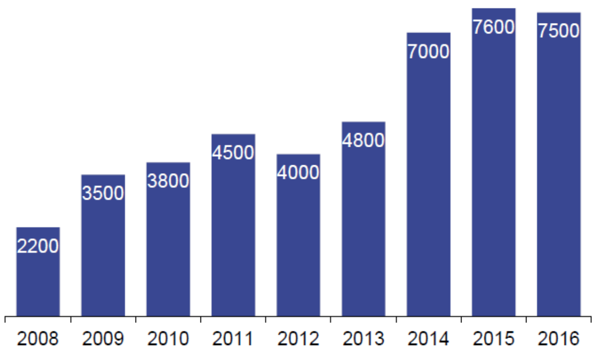
SMSFs who use ETFs typically cite a wider range of reasons for using them, especially access to overseas markets and for specific investment types.

Diversification remains the primary driving factor, with 72% of investors citing this as a reason for using ETFs.

Financial planners can tap into client demand for ETFs

Use of ETFs is widespread among financial planners, with 7,500 or 43% of Australia's financial planners currently recommending ETFs. This number looks set to grow with seven out of ten either already recommending ETFs or intending to do so in the future.

Number of financial planners using ETFs in Australia



Source: BetaShares/Investment Trends ETF Report

Financial planners who recommend ETFs are using them more extensively for new inflows, and plan to further increase their use. In terms of motivations for using ETFs, financial planners predominantly cite low cost, with diversification the second most commonly cited driver.

There remains significant opportunity for advisers to tap into consumer demand for ETFs, with only 21% of current ETF investors saying an adviser played a role in their most recent ETF investment.

Advisers also have a strong interest in actively managed ETFs, with 52% indicating they would like to use these products in the next 12 months if available to them.

Outlook for the sector

The Report projects a record 315,000 Australians will be invested in ETFs by September 2017.

The ETF sector in Australia is following in the footsteps of more mature ETF markets around the world. Recent research conducted by Blackrock indicates that 52% of individual investors and 94% of financial advisers in the US expect to invest in ETFs in the next 12 months (research from February 2017). While easy to gloss over, consider the significance of those figures - most individual investors and virtually every financial planner in the US expect to start or are already allocating to ETFs in the coming year. Contrast this to Australia where we estimate that approximately 4% of individual investors are currently using ETFs. That's a lot of potential growth!

Investors will continue to tap into ETFs for a broader range of investment needs. In line with the growth we are seeing, we project the industry will grow from the current $25 billion and reach $30-33 billion in funds under management, with approximately 250 exchange-traded products, by the end of 2017.

Ilan Israelstam is Head of Strategy & Marketing at BetaShares, a sponsor of Cuffelinks. A summary copy of the Report is available on request from betashares.com.au. This article is general information and does not address the needs of any individual.

Latest editions of BetaShares' monthly ETF Review can be accessed here.

Institutional investment in affordable housing one step closer

Adrian Harrington

The recent announcement by the Treasurer, Scott Morrison, to establish an Affordable Housing Implementation Taskforce to develop an affordable housing bond aggregator model is welcome news for affordable housing.

In a December 2016 Cuffelinks article, I set out how a bond aggregator model could work. The Australian Housing and Urban Research Institute (AHURI), which is funded by Federal and State Governments and leading Australian universities, has for years been advocating that a bond aggregator model was needed in Australia.

On the Treasurer's recent visit to the UK, he met with leading institutional investors who are providing debt via investing in bonds issued by the UK Housing Finance Corporation (THFC). They are also providing development and investment loans directly to community housing providers. Some of these institutions are investing equity into affordable housing projects. No doubt the Treasurer was encouraged to see the depth of institutional commitment to a more efficient mechanism to fund and build affordable housing.

Superannuation slow to invest in housing

Unlike their UK, US and European counterparts, Australian superannuation funds have been slow to embrace investing in affordable housing. It's therefore heartening to see a range of positive responses to the Treasurer's announcement that an Affordable Housing Implementation Taskforce (comprising federal Treasury Secretary John Fraser, former chief executive of the NSW Treasury Corporation, Stephen Knight, and Chief Executive of the Community Housing Industry Association, Peta Winzar), has been tasked with devising a plan to establish a new financial intermediary. It should attract private sector investment in new affordable housing via issuing bonds allowing community housing providers access to cheaper and longer-term debt.

The Chief Executive of the $37 billion health industry superannuation fund HESTA, Debby Blakey, said in a recent interview:

"We believe the government has an important role to play to facilitate and co-ordinate investment in social housing. The government can play an active role in developing a housing bond aggregator so institutions like HESTA can invest in them. It might be through long-dated bonds which would have an attractive income or some government guarantee on the rental return of social housing projects; long-dated bonds with terms from 15 to 20 years that had a good income would be very attractive to a fund like HESTA."

Large-scale investment critical

In the UK, the THFC has an enviable track record. From an investors' point of view it has issued more than £5 billion in bonds with a stable 'A' credit rating from Standard and Poor's and a zero default rate. But most importantly from a community perspective, it has assisted in the financing of more than 2.4 million dwellings through regulated housing associations that provide secure affordable housing.

Lending support to a similar local initiative, Wendy Hayhurst, CEO of the NSW Federation of Housing Associations said:

"… affordable housing policies must move beyond reducing pressure on real estate prices to include solutions for renters and lower income earners. Attracting large-scale institutional investment is critical to establishing the community housing sector as a third tier of the Australian housing market, between the private property development industry and public housing."

Housing underpins everything

However, the affordable housing bond aggregator model is just one component of the affordable housing solution. It is incumbent on all levels of government, the community housing providers and the institutional sector to come up with a package of tools that addresses making it easier and more affordable to either buy or rent a house. As Kasy Chambers, Anglicare Australia executive director said: "Housing underpins everything, whether health, education and general wellbeing, and there is no doubt there is a crisis in housing in Australia."

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