NATIONAL REGULATORY SYSTEM
COMMUNITY HOUSING
A joint initiative of Commonwealth, State and Territory Governments

National Regulatory System for Community Housing (NRSCH) Environmental Scan 2019

Purpose

The purpose of this Environmental Scan publication is to identify key risks facing the community housing sector and to support community housing providers (CHPs) with their strategic planning, while also providing information to the sector and stakeholders more broadly about the operating environment of CHPs.

This report is designed to be an annual publication.

A secondary but no less important purpose of the scan is that it provides Registrars with intelligence on emerging trends and risks to the sector. The scan will support the focus of Registrar's attention and resources on the risks of greatest importance, and help guide future compliance assessments through identifying issues or business circumstances that may be examined through for example, deep dives.

Introduction

This is the first environmental scan report published by the National Regulatory System for Community Housing (NRSCH) Registrars.

A key role and responsibility of Boards and executives within the NRSCH is ensuring effective governance and risk management of your organisations (as registered CHPs).

Even if a CHP's aims and objectives are not evolving, the sector and policy environment is continuing to change. Boards and executive teams should be regularly assuring themselves that they have the appropriate skills to manage their business in this environment of change.

In contrast, the regulator's role within the NRSCH is to seek assurance that your organisation has identified the risks to your business and that you are effectively managing those risks.

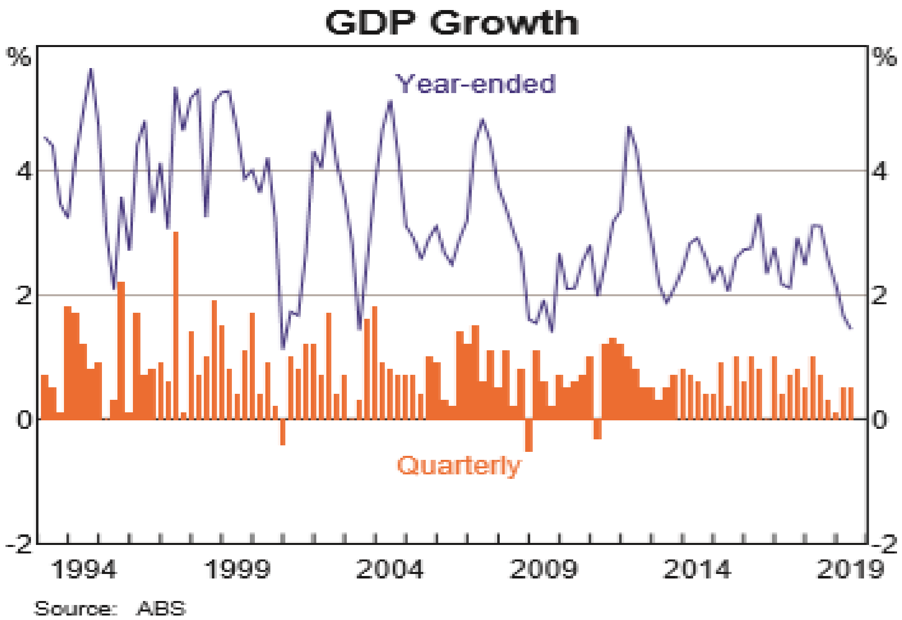
The sophistication of the Environmental Scan will improve over time as sector benchmarking, property level data collections and profiling to provide new insights for the registrars that will also be useful for CHPs.

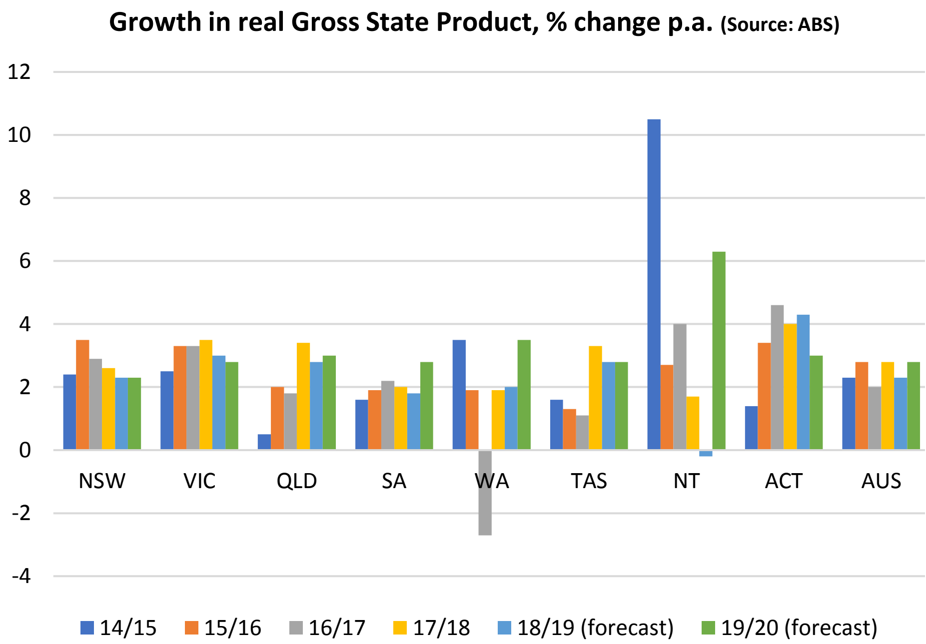
In recent years, registered CHPs have enjoyed a generally benign economic climate. However, many CHPs are now facing an increasingly complex operating environment as they diversify into a wider range of markets. Every organisation will face its own unique combination of issues, and it is vital that Boards understand and can manage the risks particular to their own businesses. This scan does however seek to identify a number of key environmental factors that are expected to become increasingly important to a large proportion of the community housing sector.

Registrars will continue to seek assurance on registered CHPs' risk management through annual or biennial compliance assessments and will reflect that level of assurance through the executive summaries published on the NRSCH website.

Economic environment

Recognising and responding to broader economic trends is a key challenge for any sector. It is particularly important in community housing given legislative constraints imposed on providers (e.g. rent charged to tenants, enterprise bargaining agreements (EBAs), thereby limiting their ability to implement strategies that may be available to landlords in the private sector.





Low and stable economic growth in the near term

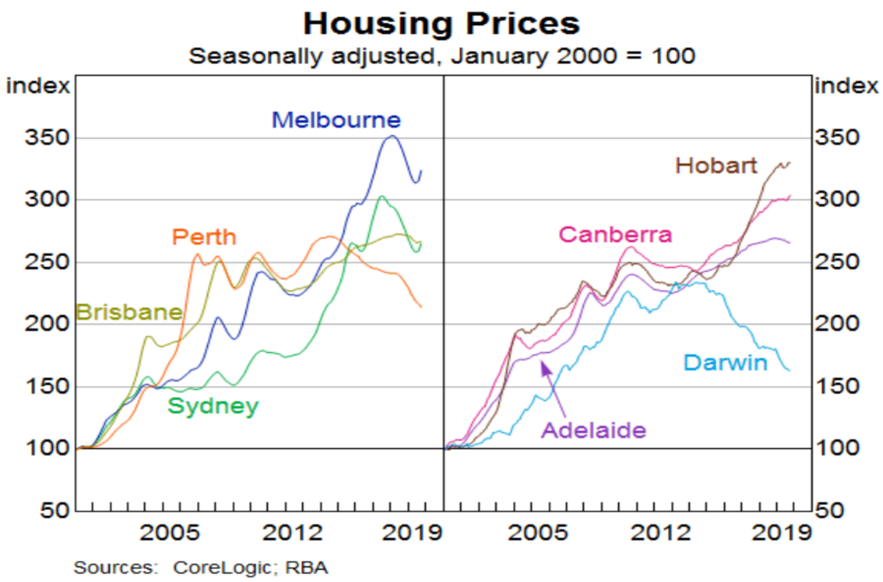
Australian economic conditions have continued to soften over the past year, with expectations of above trend growth failing to eventuate.

The domestic economy is likely to exhibit low and stable growth in the near term. The Reserve Bank of Australia anticipates:

- Annual GDP growth of 2.7% to June 2020, rising to 3% to June 2021
- Inflation pressures remain subdued, but inflation was expected to increase gradually to be a little over 2 per cent over 2021
- A sustained low cash rate – with inflation forecast to remain below the target range (of 2-3% across the business cycle) across the next three years.

Major housing markets have started to steady

Established housing market conditions have steadied in Sydney and Melbourne over the past couple of months, with economists pointing to changes to APRA's mortgage serviceability requirements and lowering of the cash rate as important factors. While prices have risen, and the pace of growth in housing prices has also picked up in Canberra, Hobart and to a lesser extent Brisbane, housing turnover has remained low.



But new dwelling activity remains weak

While established housing markets have begun to turn around, the same cannot be said for new dwelling activity which remains weak. The Reserve Bank has noted that the current contraction of the residential construction sector is expected to continue for some time, and that while the underlying demand for housing through population growth may lead large developers to retain employees during the expected trough in activity over the next year, that "the outlook for smaller contractors … is not so great in the period ahead". These warnings shine a light on the importance of Boards assuring themselves of the due diligence undertaken into builders involved in construction works.

It is important that registered providers and their boards continue to have oversight and awareness of those risks that are within their direct control and have a robust approach to stress testing. This should take account of a wide range of scenarios and different risks (both those in their direct control, and those which are not, but will require mitigation) that could take effect in combination for both its social and non-social housing activities.

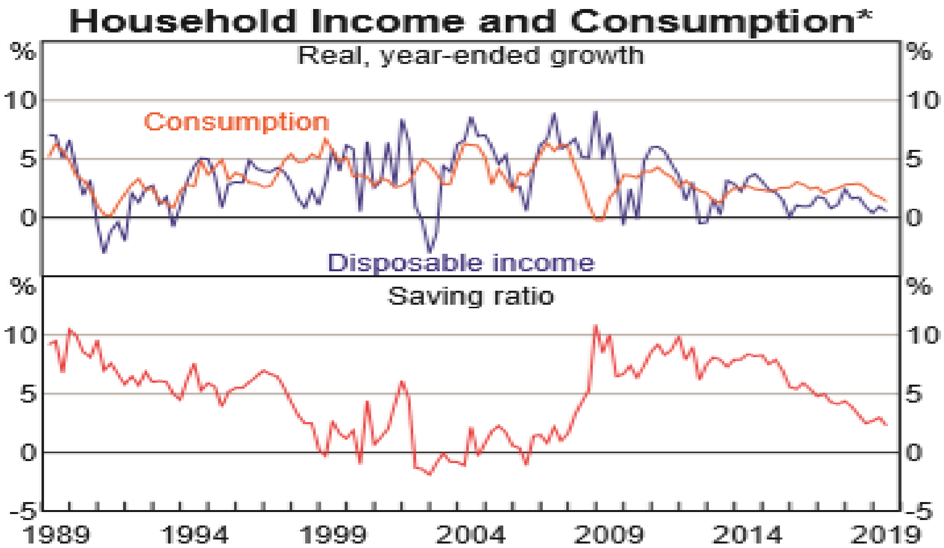
Employment growth is expected to moderate

The labour market has remained steady, with unemployment remaining around 5.2 per cent over recent months, and the participation rate at an all-time high.

The Reserve Bank has however indicated that it expects that unemployment outcomes over the following couple of years are likely to be short of its own goals, necessitating a continuation of low interest rate settings for an extended period aimed at continuing to move the economy towards full employment.

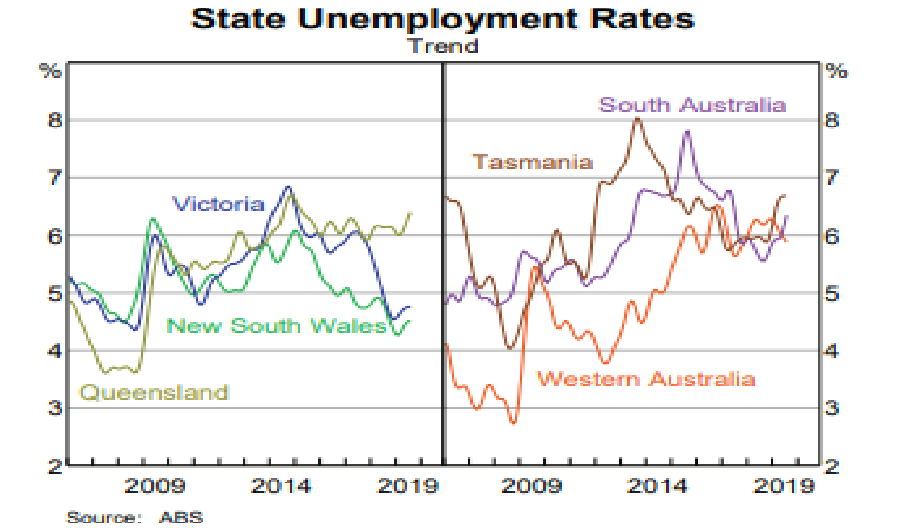
With employment growth forecast to slow moving forward, and few indications that wage pressures are building, wages growth expectations for 2020 and 2021 have moderated. Employment trends can impact CHPs in a number of ways, from input costs for staff or contractor expenses to earnings expectations related to income-linked rents.

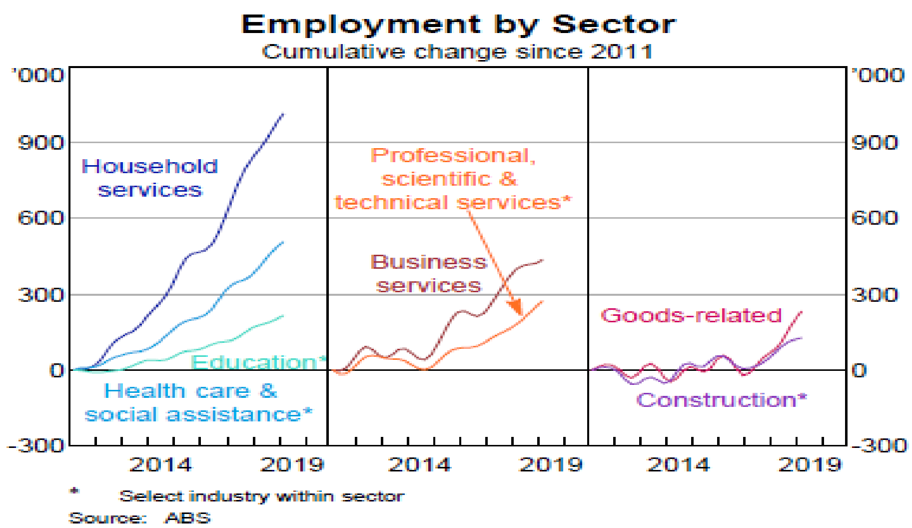
Low wages growth is also expected to continue dragging on real household disposable income growth, while the low-and-middle income tax offset is expected to boost household incomes in last quarter of 2019. The subdued forward outlook for household incomes is expected to maintain a brake on household consumption over the forecast period.



* Household sector includes unincorporated enterprises; disposable income is after tax and interest payments; saving ratio is net of depreciation

Sources: ABS; RBA





Global growth expectations trending down

Global economic activity remains sluggish, and while downside risks have intensified over the year the outlook remains reasonable.

The key risks to this short-term outlook remains the ongoing trade tensions between the United States and China hurting business sentiment and confidence globally, and to a much lesser extent risks surrounding an orderly Brexit.

The International Monetary Fund forecasts the global economy to expand by 3.0 in 2019, before picking up to 3.4 percent in 2020. This forecast pick-up in growth is noted as being precarious by the IMF and presumes progress in resolving trade policy differences and stabilisation in currently stressed economies.

While it is not expected that CHPs will necessarily have much international exposure, the crystallisation of key risks overseas could impact on financial market sentiment, tighten financial conditions or result in increased costs for CHPs undertaking development projects.

Government policy environment

With the two elections held in 2019 resulting in the continuation of governments in NSW and at the Commonwealth, and with no government elections until 31 October 2020 (when the Queensland state election is scheduled) the Government policy environment remains steady.

The re-election of the Morrison Government at the Commonwealth election held on 18 May 2019 resulted in minimal changes to the Commonwealth Government policy settings impacting on the sector.

The re-election of the Berejiklian Government at the NSW election held on 23 March 2019 has seen the continuation of social and affordable housing settings in that jurisdiction, with the only relevant election commitment to halve street homelessness across the state by 2025, as part of the global agreement signed by the Government and service providers.

With Queensland and the Northern Territory heading to the polls in 2020, consistency of policy settings at both the Commonwealth and State level appears likely in the short term.

Housing policy remains conducive to growth

The housing policy environment remains broadly conducive to community housing growth, with the implementation of growth-based programs in the majority of participating jurisdictions. CHP Boards should be aware of jurisdictional policy and program changes and be considering what those changes mean for their organisation.

Australian Capital Territory	New South Wales
ACT Housing Strategy October 2018 • Government commitment to release 15% of its annual indicative land release program to affordable, community and public housing • Support culturally appropriate public and community housing accommodation options and support programs for ATSI people	• The Social and Affordable Housing Fund is expected to deliver 3,400 additional social and affordable housing dwellings by 2023 • The transfer of around 14,000 social housing tenancies to CHPs under the Social Housing Management Transfer Program • Providing floor space incentives for developments which contain affordable housing through the State Environmental Planning (Affordable Rental Housing) 2009 • Facilitating other incentives for developments which contain affordable housing through negotiated planning agreements

Northern Territory

The NT Government is committed to providing opportunities to transfer government service delivery to Aboriginal communities and organisations, based on their aspirations as part of a whole of government policy agenda to support Local Decision Making.

Local Decision Making and community engagement are key principles underpinning the ten-year, $1.1 billion Remote Housing Program and the ‘Building our Communities, together with the Town Camps Reform Framework 2019-2024’. Under these initiatives, the Aboriginal community housing sector will be strengthened and supported to grow through capacity building, regulation and transfer of housing and asset management when organisations are ready.

The reform frameworks seeks to:

- Where suitable, transition housing stock to Aboriginal controlled housing organisations when the organisations are ready.
- The capacity and capability of Aboriginal controlled housing organisations is improved through working towards appropriate NRSCH registration.
- Aboriginal controlled housing organisations share good practice and build their capability.
- Investment into the workforce across the Aboriginal community housing sector.

Queensland

Through Partnering for Growth, which is a key initiative of the Queensland Housing Strategy Action Plan 2017-2020, QLD is:

- developing a new person-centred and place-based housing response through a single community housing program and new affordable housing setting
- Working with Providers to agree 5 year development plans aimed at growing social and affordable housing, with supporting financing plans that allow for the consolidation of provider equity to better enable Providers to obtain finance
- Providing capital assistance to build new social housing through the Housing Construction and Jobs Program

A second housing action plan will be delivered in 2020.

Western Australia

WA Housing Strategy 2020-2030 is currently in development and due to be delivered in the first half of 2020.

South Australia

- Around 5,000 dwellings and their households have had their tenancy management transferred to a registered CHP since 2015-16, with 4,000 of those transfers occurring in 2017-18
- The development of a new Housing, Homelessness and Support Strategy has taken place over 2019, 2020 will have a strong focus on working with stakeholder in the broader housing sector to implement the broad range of actions included in the strategy.

Tasmania

- An overall total of 1155 new homes to be delivered by 30 June 2023, of which 372 new homes targeted under the initial Tasmanian Action Plan
- $30 million for projects in partnership with CHPs to deliver new dwellings under the Hobart City Deal

Commonwealth

- The National Housing Finance and Investment Corporation (NHFIC) will be operating a First Home Loan Deposit Scheme that will enable up to 10,000 first home buyers a year to purchase a home with a deposit of as low as 5 percent. The Scheme will commence in 2020.
- A new research function within NHFIC will conduct comprehensive research into housing demand, supply and affordability in Australia, including current and potential future gaps between housing supply and demand.
- $78 million for emergency accommodation and Safe at Home programs for women and children impacted by family violence, and $82 million for frontline services.

Social housing management transfers

Historically, much of the growth of the sector can be attributed to the transfer of management rights of public housing. CHPs that succeed in tenders for management rights over previous public housing should do their due diligence on any transfer deal to ensure they understand the implications for their business of accepting a transfer, particularly in areas such as dwelling quality and the potential repairs to transferred properties.

This trend has certainly accounted for much of the recent growth of the sector, including through:

- Better Housing Futures in Tasmania (stock transfers) 3900 homes managed by CHPs under the Better Housing Futures initiative
- The transfer of 5000 tenancies through BPSC & ROSAS programs in South Australia
- Over the past two years, Family and Community Services has transferred the tenancy management of around 14,000 social housing tenancies to CHPs, including the delivery of private rental assistance products under Housing Pathways.

While these transfers are not expected to have adjusted the tenant profiles of CHPs on aggregate, historically such transfers have had financial and operational impacts on individual providers particularly in the area of increased maintenance and rectification costs.

NRSCH review offers opportunity for positive changes

On 17 December 2018, the NRSCH Review was announced and a discussion paper released for public consultation. The Review will seek to ensure the NRSCH continues to be relevant to a growing and evolving community housing sector, and that providers deliver quality tenant outcomes.

The key themes arising from consultations undertaken through the Review to date have included:

- It is recognised that regulation of the community housing sector is required, but that reform is required;
- Improved transparency and engagement between the registrars and the sector will improve compliance
- The role of tenants needs to be considered
- Regulatory burden remains a challenge
- Greater regulatory flexibility will support an evolving sector.

An Options Paper outlining potential NRSCH reforms, informed by public submissions and consultation from the first stage is expected to be released in the coming months, before a Final Report detailing reform recommendations is presented to Housing Ministers in 2020.

Working in parallel with the broader NRSCH Review, the NRSCH National Office with the assistance of state and territory Registrars and other officials, have commenced a review of the data reporting needs of the NRSCH (the Data Review). The Data Review is discussed further under the Technology Trends part of this Environment Scan.

CHPs should remain engaged with the NRSCH Review and Data Review processes as they progress, including maintaining regular communication with sector peak bodies, in order to ensure these processes benefit from the CHP's experience and perspective. They should be aware that possible outcomes of these reviews may include legislative or policy changes that could have implications for the relationship between CHPs and the NRSCH, and ongoing monitoring and engagement will assist providers to better adjust to any consequential changes.

Overlapping human services policy

Royal Commissions into human services provision

With the increasing diversification of CHPs as part of broader human services organisations, the boards of some registered providers are required to monitor, and engage as required, with additional Government oversight, including current and future Royal Commissions and inquiries.

Of particular importance for providers that form part of a broader human services organisation will be:

- The Royal Commission into Aged Care Quality and Safety which was established on 8 October 2018. The Commissioners are required to provide an interim report by 31 October 2019, and a final report by 30 November 2020.
- The Royal Commission into Violence, Abuse, Neglect and Exploitation of People with Disability, or 'Disability Royal Commission' which was established on 4 April 2019. The Commissioners are required to provide an interim report no later than 30 October 2020, and a final report by no later than 29 April 2022.

A feature of the Royal Commissions to date has been the increasing expectations of the community that there are substantive sanctions for non-compliance, that enforcement powers are used as a first rather than final step, and the ongoing need to improve transparency of regulatory outcomes.

In addition to the deliberations of these Royal Commissions, CHPs may also be subject to changing regulatory obligations in:

- Aged care – where the latest Commonwealth Government Ministerial Statement of Expectations sees the newly formed ACQSC working on the development and implementation of aged care reform initiatives including:

    - A single charter of rights and responsibilities for aged care consumers
    - The implementation of improved risk profiling and information sharing
    - The implementation of an open disclosure framework to support providers to meet the requirements of the standards, as well as the development of plain-English audit reports
    - The development of a resource model for aged care regulation.

- Disability services:

  - The Australian Government is extending the National Disability Advocacy Program (NDAP) to include individual advocacy support for people who need extra support to engage with the Disability Royal Commission.
  - Advocacy support is for people with disability (or family members or carers acting on their behalf) who may have difficulty in communicating or understanding how to engage with the Commission.

- Charities regulation:

  - A legislative review of the Australian Charities and Not-for-profits Commission undertaken in 2018 has led to 30 recommendations for consideration by the Australian Government.
  - A 2017 review of the CATSI Act by the Office of the Registrar of Indigenous Corporations (ORIC) led to proposed amendments to the Act to improve transparency for members, improve options for the Registrar to respond to lower-level cases of non-compliance, and reduce red-tape for small corporations. With the proroguing of the 44th Parliament, the Bill lapsed.

Demand trends

Affordable housing needs are growing

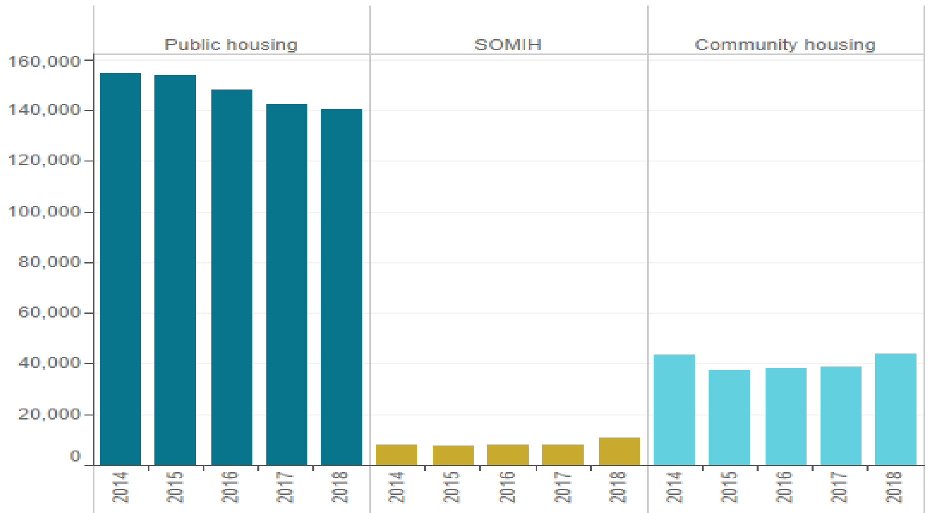
Demand for housing assistance is high around Australia, with large waiting lists resulting in some individuals waiting up to 10 years for a social or community housing dwelling.
The Productivity Commission has found that:

- More than 400,000 households in 2016 are eligible for, but cannot access, social housing.
- 2/3 of low-income private renter households in 2017-18 spent more than 30 percent of their income on rent, while nearly half have less than $500 a week to meet other expenses.
- 225,000 low-income private renter households in 2017-18 spent more than half of their income on rent, while around 170,000 have less than $250 a week to meet other expenses.

Utilising the Australian Bureau of Statistics population projections, AHURI has estimated that addressing the current deficit of 'manifest' and 'evident' available social housing and future need will call for the construction of around 730,000 new social dwellings over the next 20 years, equating to an annual average growth of 5.5 per cent over the existing stock.

These studies indicate that the current strong demand for social and affordable housing is expected to remain for the foreseeable future.

Total number of applicants on waiting list (excluding applicants for transfer), by social housing program, at 30 June 2014 to 2018
Australia

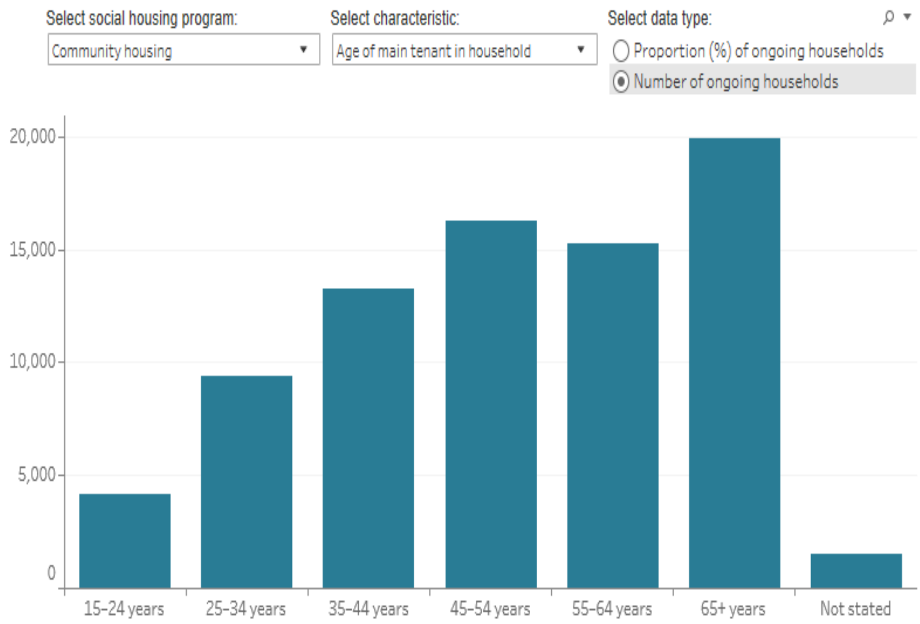


Notes:
1. Data for Indigenous community housing were unavailable
2. Some data were not available or not applicable for some housing programs and/or in some states and territories. See the data source for more information.

Measure:
Total applicants on waiting list (excluding applicants for transfer)

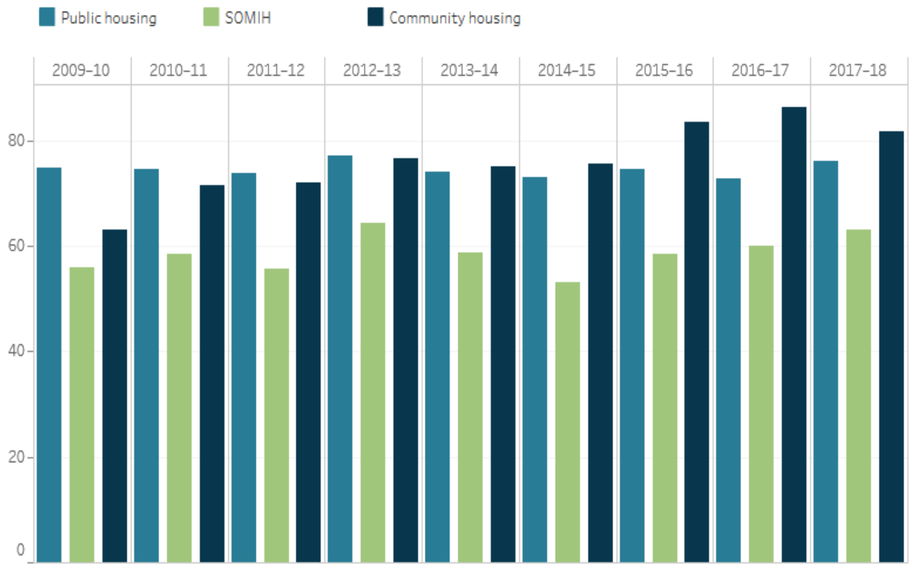
Source: AIHW National Housing Assistance Data Repository, 2019
https://www.pc.gov.au/research/ongoing/report-on-government-services/2019/housing-and-homelessness
Latest data: 2017–18 (annual)

Figure TENANTS.4: Number of ongoing households in community housing, by selected characteristics, at 30 June 2018

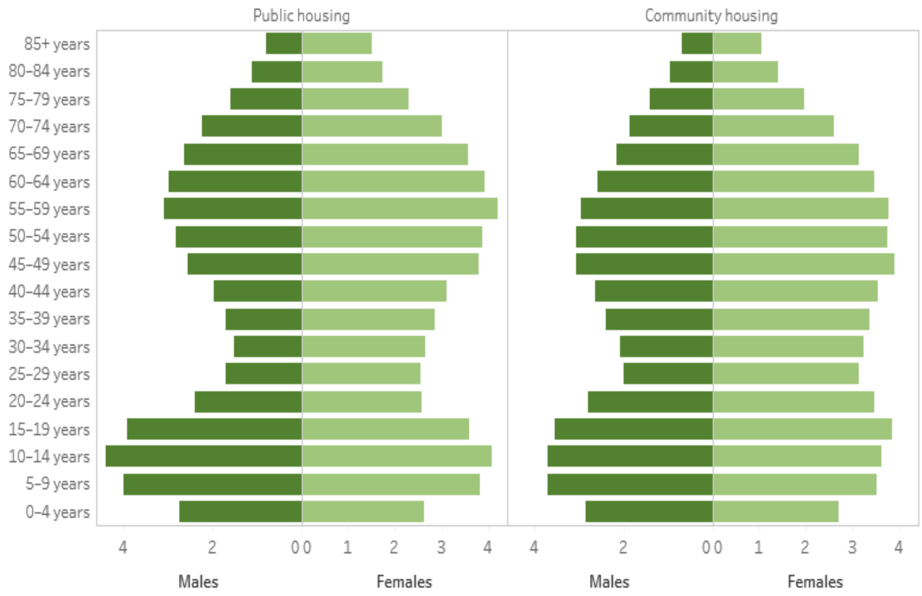


Source: AIHW

Figure PRIORITY.2: Proportion (%) of newly allocated households in greatest need, by social housing program, 2009–10 to 2017–18



Source: AIHW



Source: AIHW

While the demand for low-cost housing is manifest, the financing to enable the supply of subsidised housing at scale is not. This is leading CHPs to deliver housing across the housing needs continuum in order to improve project level financial viability through cross-subsidy, as well as help meet overall social and tenure mix objectives.

Providers' tenant mix is continuing to change

Based on the available data in 2017–18, AIHW has estimated that of the new households in community housing in greatest need where the main reason was known:

- almost 4,700 (43%) households were experiencing homelessness, an increase from 3,100 in 2013–14
- around 6,100 (57%) households were at risk of homelessness, an increase from 2013–14 (53%, or 3,400 households)

Consistent with broader demographic trends around Australia for an aging population, the tenant profile of CHPs is increasing in the 45-65 age brackets particularly new women tenants. Over the past 10 years the tenant mix has changed, with tenants with more complex needs are now the majority (disability, aged, homelessness etc) which places further pressure on CHPs to support these tenants towards sustainable tenancies.

NDIS is providing more people with disabilities the opportunity to live on their own.

This is likely to impact on provider's cost drivers, and income expectations, due to tenant needs.

Tenant environment

Increasing energy costs for tenants

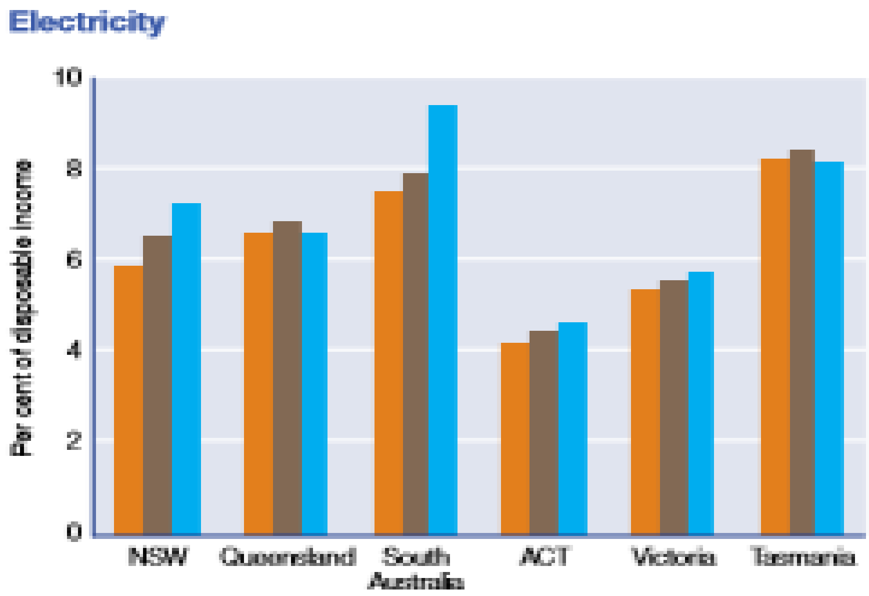
High energy costs and poor building energy efficiency can have significant financial and health effects on households, including households in community housing. As indicated in the latest Australian National Outlook prepared by the CSIRO, energy poverty (where individuals are unable to access energy needed for well-being) remains a problem with electricity costs for low income households as a percentage of disposable household income growing to as much as 12.4% in 2017-18. This is disproportionately affecting households in the lowest income bracket, with around 1% of electricity customers being disconnected for failure to pay in Queensland, South Australia and New South Wales in 2017-18.

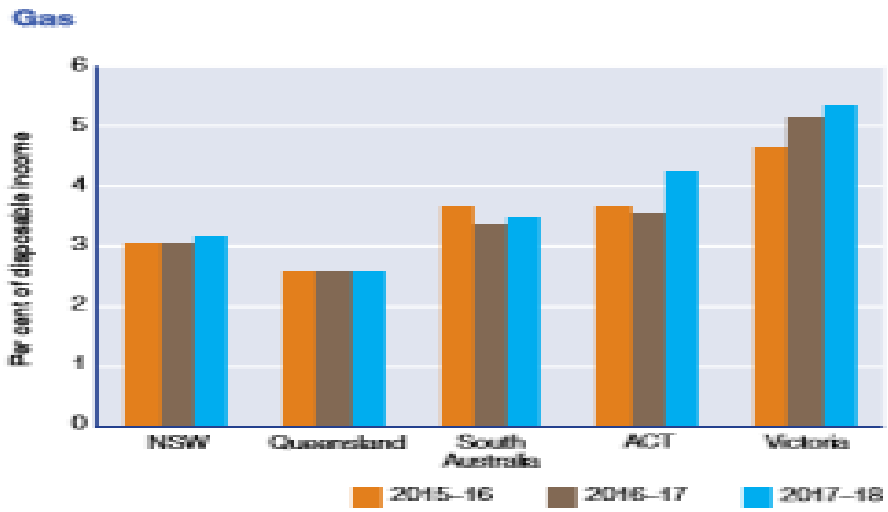
There are many energy efficiency improvements with payback periods of five years or less that can be during the building phase and to existing dwellings. While energy efficiency improvements involve upfront costs, more energy efficient community housing would lower energy bills and increase thermal comfort, improving households' financial, health and social outcomes.

Clean energy solutions can include rooftop solar, battery installations, heat pumps, additional insulation, double glazing, smart meters, LED lighting and energy efficient white goods.

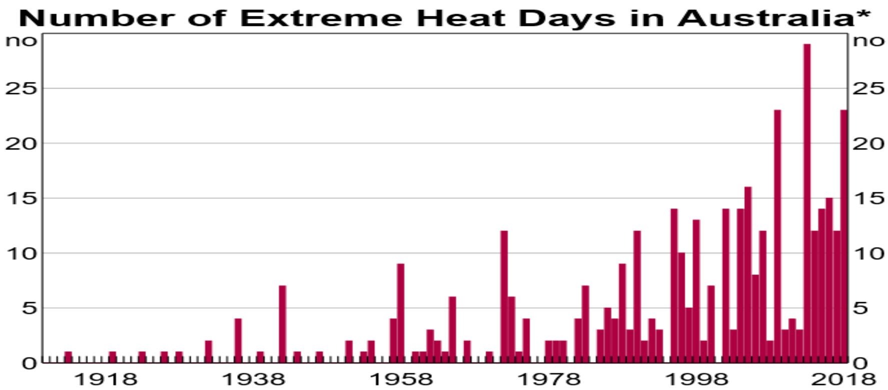
The Clean Energy and Finance Corporation (CEFC) is providing tailored long-term finance for energy efficient community developments, to deliver the benefits of clean energy to owners and tenants, as well as tackle household emissions. CEFC finance is available to support the construction of new market-leading energy efficient community housing, as well as energy efficiency retrofits to existing homes.

Energy bill burden on low income households 2017-18





Source: AER, Annual Report on Compliance and Performance of the Retail Energy Market 2017-18, December 2018



* Number of days each year where the Australian area-averaged daily mean temperature is extreme; extreme days are those above the 99th percentile of each month from the years 1910–2018; these extreme daily events typically occur over a large area, with generally more than 40 per cent of Australia experiencing temperatures in the warmest 10 per cent for that month

Source: Bureau of Meteorology State of the Climate report, updated to 2018

Welfare changes could impact on tenant incomes

The Australian Government has committed to extending its income data-matching activities between the Department of Human Services and the ATO to enhance the integrity of social welfare payments with tranche three of the Welfare Payment Infrastructure Transformation program.

Tranche three of the WPIT program will extend the application of the Social Welfare Debt Recovery program from Austudy and Youth Allowance recipients to those claiming age, disability, and job seeker pensions, as well as carer payments.

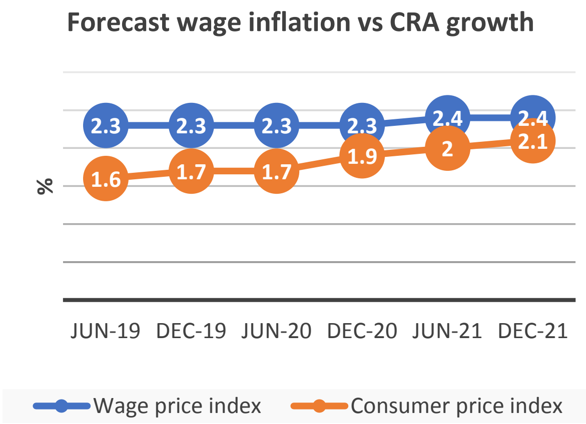
While these arrangements are not expected to have had much impact on provider cash flows now, the expansion of the program to cover a broader number of welfare payment recipients may see debt recovery payments impacting on a large number of tenants. This is a slowly unfolding process and will be monitored over the ensuing compliance periods.

Operational trends

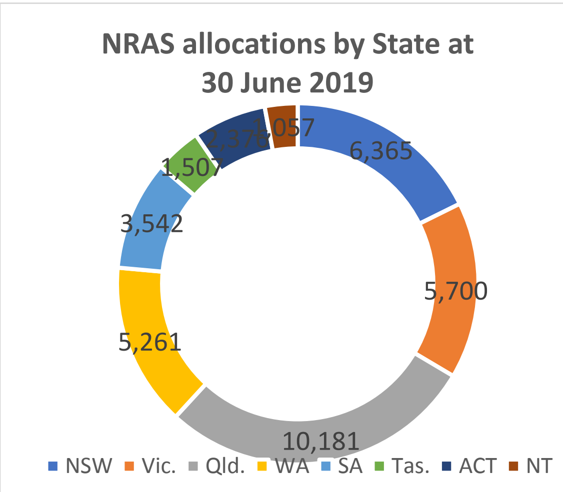
National Rental Affordability Scheme (NRAS) cessation

The cessation of NRAS subsidies between 2018 and 2026 will increase income pressures on a small number of providers across the NRSCH, with the most significant impacts in NSW and Queensland. The NRAS allocates financial incentives to organisations that provide people on low to moderate incomes with an opportunity to rent homes at a rate that is at least 20 percent below market value rent.

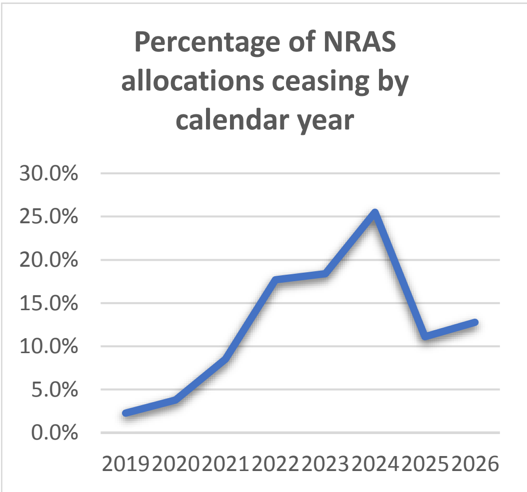
Registrars' examination of the approaches that CHPs are taking to the loss of subsidy to date[1] have indicated that providers are taking significant steps with respect to planning, risk mitigation and identification of potential impact. Registrars will continue to monitor the execution of providers' plans to manage this loss and the impact that the cessation of the subsidy has on affordable housing tenants.



Source: RBA



Source: NRSCH



Source: NRSCH

[1] https://www.nrsch.gov.au/news_and_events/nras-and-the-community-housing-sector-a-national-report

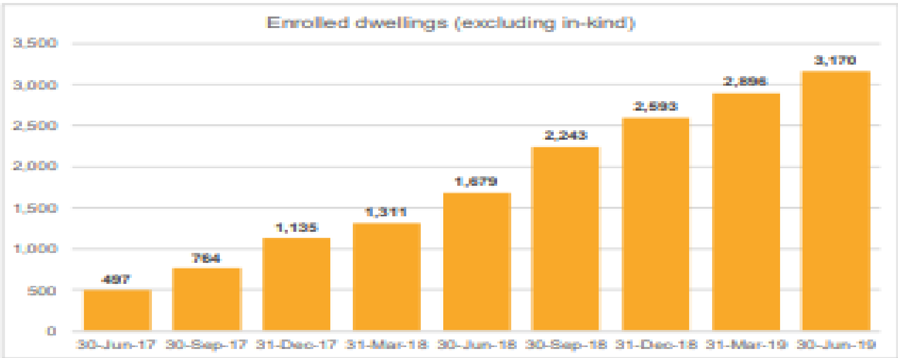
Slow growth of income linked rents

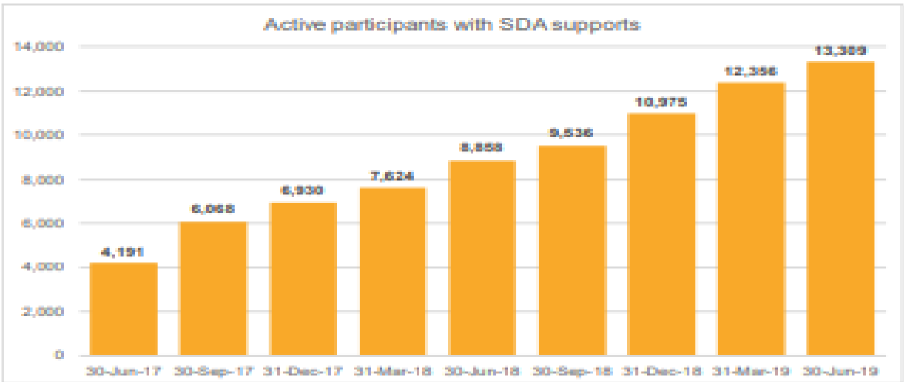
In all participating jurisdictions, a key source of income for providers is Commonwealth Rent Assistance (CRA) which tenants in social and affordable housing are required to pass through providers via rent payments.

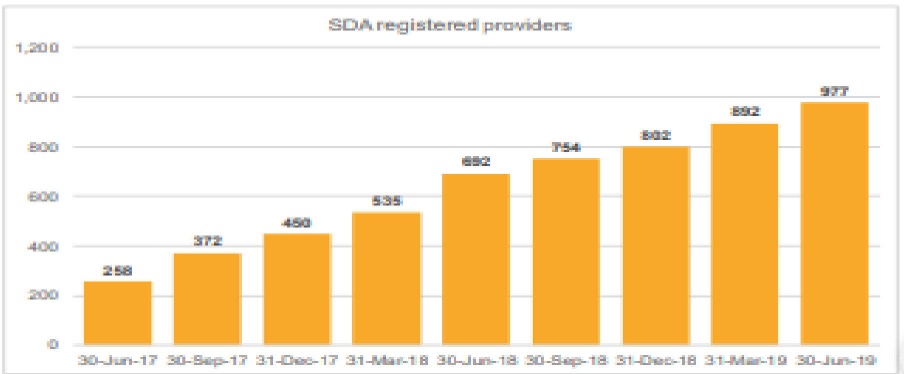
The Department of Human Services (DHS) updates Rent Assistance rates on 20 March and 20 September each year, in line with the Consumer Price Index. As indicated above, inflation is expected to remain subdued for the foreseeable future. The continued divergence between the growth of CRA over the next couple of years and providers' expenses presents a growing source of pressure for providers necessitating ongoing efforts to improve productivity.

Indexation rates can significantly alter long-term revenue projections, particularly across a 30-year timeframe.

Changes in Specialist Disability Accommodation by quarter







Source:
National Disability Insurance Scheme, COAG Disability Reform Council Quarterly Report, 30 June 2019

Specialist Disability Accommodation (SDA) presents an opportunity

As of 1 July 2019 the National Disability Insurance System is available in every region of Australia. The NDIS's approach to housing is changing the way some people with disabilities find housing and the way that providers create and manage housing for people with disability.

SDA funding is provided to a participant, not a dwelling, and a participant can move from one dwelling to another. The participant can then use that funding to find a dwelling to move into that is consistent with their goals and support needs.

It is forecast that only about 6 percent of Australians that can access an NDIS package will get any assistance with accommodation through SDA payments.

The principle risks on the return in SDA property are vacancy risk, and the failure to adhere to the strict compliance requirements set by the National Disability Insurance Agency (NDIA). Ensuring that you understand the detailed specifications and payment arrangements in SDA requirements is key to a viable outcome.

The NDIA continues to work with the Department of Social Services on delivering a package of reforms to SDA, following a review of the SDA Pricing and Payments Framework by the Disability Reform Council (DRC) in 2018. The reforms include several key initiatives underway which will further strengthen and improve the SDA market, provide investors with greater confidence and enable varied and innovative market growth for participants requiring SDA.

Operational trends and risks

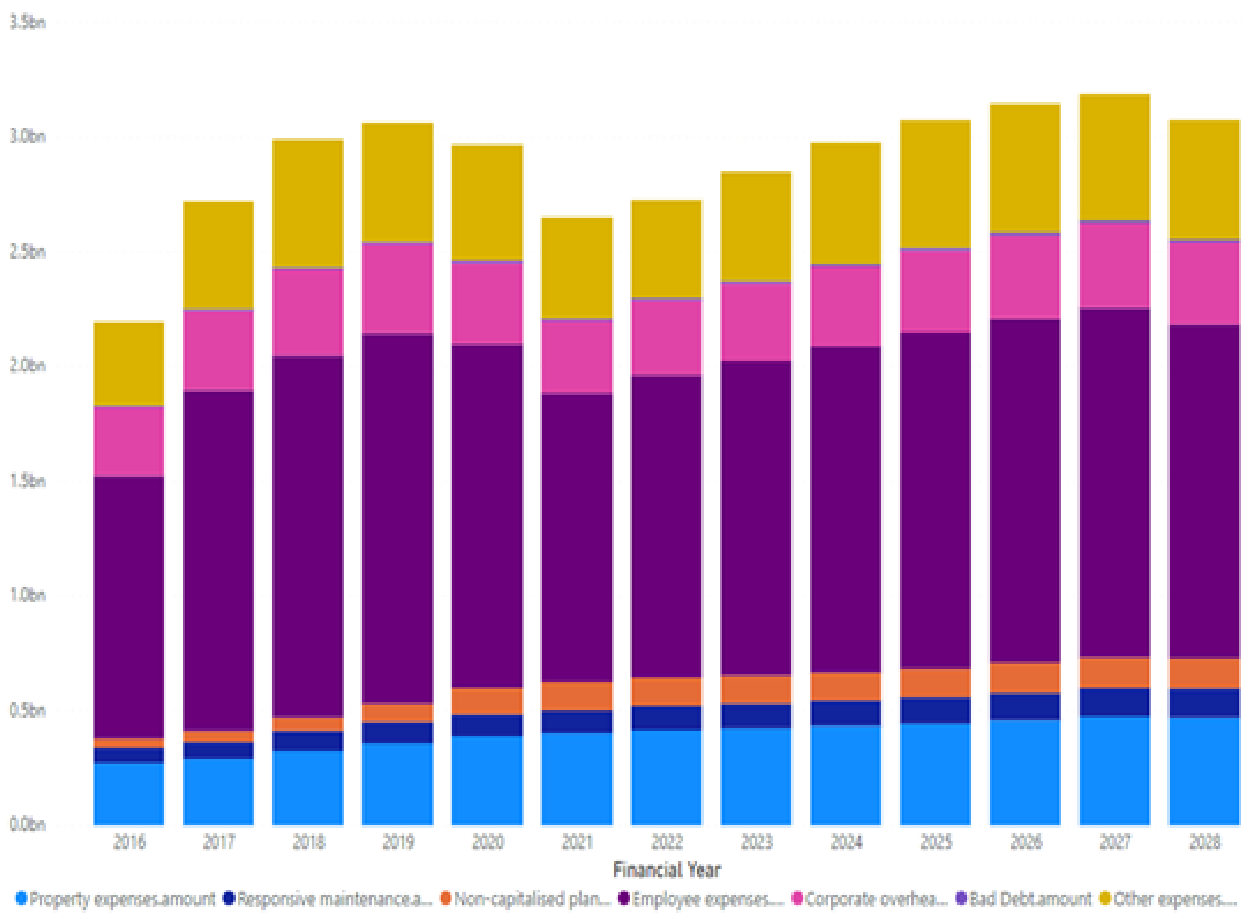
Expense trends

Employee costs

As indicated in the economic drivers section of this paper, wage growth is currently subdued and forecast to remain low with the RBA indicating that there are no indications that wage pressures are building in the economy.

Subdued wages and strong employment growth aren't expected to have significant impacts on community housing tenants or waiting lists. Registered CHPs, however, need to factor in rising wage costs from the phase-in of increases under the Social, Community Home Care and Disability Services Award rates in December 2019, as well as increasing competition for staff with the maturation of the NDIS.

Source: NRSCH



Source: NRSCH

Review of the model Work Health and Safety (WHS) laws

A review of the content and operation of the model WHS laws was conducted in 2018. The review was completed in December 2018 and the report has been provided to WHS ministers for their consideration. WHS ministers are yet to determine when the report will be publicly released. The Accreditation register can be viewed on the Office of the Federal Safety Commissioner website www.fsc.gov.au.

Development trends

Construction costs

As noted in the Economic trends section of this Paper, the outlook for the construction sector remains weak. While this may present opportunities for obtaining contractors at competitive prices, CHPs should remain alive to the potential of, and scenario plan for, one or more contractors collapsing during a construction project.
Over the last twelve months:

- non-residential construction costs rose 2.3%
- While inputs to house construction rose 1.8%

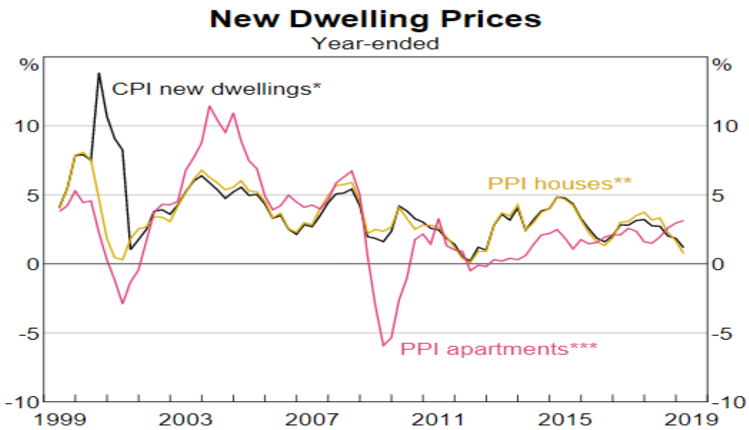
These costs are above the inflation rate.

Private market sales and rents

The sector is progressively increasing its involvement in the development of new properties for outright market sale. It will be important that providers can manage this increase in sales risks and ensure that business plans are resilient to any shortfall in receipts.

It is important that increasing exposure to private market sales or rents represent a pro-cycle assets and incomes (that is, the value of the assets move consistent broad economic trends) rather than social housing assets which traditionally have not been affected in the same way by the economic cycle.

The housing price cycle is very different across the states, across cities within states and across suburbs within cities. Price cycles reflect different population dynamics, particularly migration flow, as well as differences in employment, income and the cost of housing.



* Adjusted for the tax changes of 1999–2000; attached dwellings included from March 2017 onwards
** 'Output of house construction' series
*** 'Output of other residential construction' series; includes apartments and other attached dwellings
Sources: ABS; RBA

The complexities of project initiation and financing required providers to have strong in-house development knowledge, and project management and financial expertise to achieve successful projects and effectively manage the risks associated with development.

Building industry changes

Recent high profile incidents of poor building practices resulting in cracking of residential towers, such as Opal Towers and Mascot Towers in Sydney, and the Neo200 building in Melbourne, have highlighted the need for providers to remain vigilant in regards to new construction (financial and reputational impacts of poor building practices, as well as impacts on residents)

Across all jurisdictions Building Ministers have agreed to all of the recommendations of the Shergold Weir Building Confidence report, even if only in-principle, including recasting and strengthening the Australian Building Codes Board. The progressive implementation of these recommendations will occur at different times across jurisdictions, with likely impacts on the costs of construction as various parties throughout the building and construction industry adjust to new requirements.

Registered providers should be aware of the changing environment within their State and how those changes will affect their business. The cost implications of those changes should be understood, noting that those costs will continue to feed into trend growth in input costs for new attached dwelling construction.

Accounting changes

Changes to the accounting standards impacting on Not For Profits were announced by the Australian Accounting Standards Board (AASB) in late 2016, with a requirement for all Not For Profits (and therefore the majority of CHPs) to have fully implemented the changes in FY19/20. This includes:

- AASB 15 Revenue from Contracts with Customer will replace AASB 118 Revenue, AASB 111 Construction Contracts
- AASB 16 Leases will replace AASB 117 Leases
- AASB 1058 Income of Not for Profit Entities will replace AASB 1004 Contributions

CHPs may need to consider whether to apply these changes to their FY18/19 results retrospectively in their FY19/20 Audited Financial Statements.

As indicated in *Changes to the Financial Performance Report* on 10 September 2019, Registrars encourage CHPs to seek independent, professional advice on the implementation of the new standards that are specific to their situation and review whether there are any material impacts arising from their adoption.

Insurance costs

Climate change and its effects on the frequency and intensity of extreme weather events is exposing CHPs and their tenants to risks and costs that will rise over time, if not addressed. The implications of climate change are particularly relevant for insuring buildings and the contents within them.

The RBA has noted that the “inflation-adjusted insurance claims for natural disasters in the current decade have been more than double those in the previous decade.”

The implications of these increased costs to providers is most evident in Northern Australia where insurers have responded to increasingly frequent environmental disaster events by increasing premium costs or refusing coverage. An ongoing review by the Australian Competition and Consumer Commission into insurance markets in Northern Australia has resulted in 28 recommendations that the ACCC considered would improve how insurance markets work and which would achieve better outcomes for consumers. The Commonwealth government is currently considering its response to the recommendations.

Markets have also responded accordingly and have begun to examine the potential of climate risk on their customers (https://www.iag.com.au/sites/default/files/documents/Severe-weather-in-a-changing-climate-report-011119.pdf)

Pressure on Providers in regions with high exposure to climate change impacts to maintain insurance coverage are likely to grow as insurers’ and regulators’ understanding of climate risks improve.

Strategic risks

Governance trends

As organisations with a social purpose, and often charitable status, registered CHPs should be aware of the high governance standards expected of them by Registrars and their broader stakeholders.

While CHPs are not required to be not-for-profit entities, the number of for-profit entities is currently very small though expected to grow in some jurisdictions moving forward.

Community expectations around the governance of not-for-profits remain high, with increasing media reporting on misconduct and poor governance practice in the NFP sector through the child sexual abuse royal commission and the aged care inquiry in particular. Within this environment, the Australian Institute of Company Directors released the 2nd edition of their Not-for-profit Governance Principles in January 2019.

While the NRSCH governance standards represent a base requirement for all registered providers, CHPs are encouraged to work towards best practice. The NFP Governance Principles provide a detailed, practical and principles-based framework to help not-for-profits to achieve good governance. A suite of supporting materials and content to assist users of the Principles are available free of charge on the AICD website.

The Principles seek to go beyond what may be considered a minimum standard of governance, and aim to encourage organisations to strive for and achieve good governance. The Principles should be viewed as complementary to, and building on, the Australian Charities and Not-for-profits Commission Governance Standards.

Diversification

As registered providers face new pressures, boards have increasingly taken the strategic decision to diversify and look for new and innovative ways to meet housing demand and deliver more efficient services.

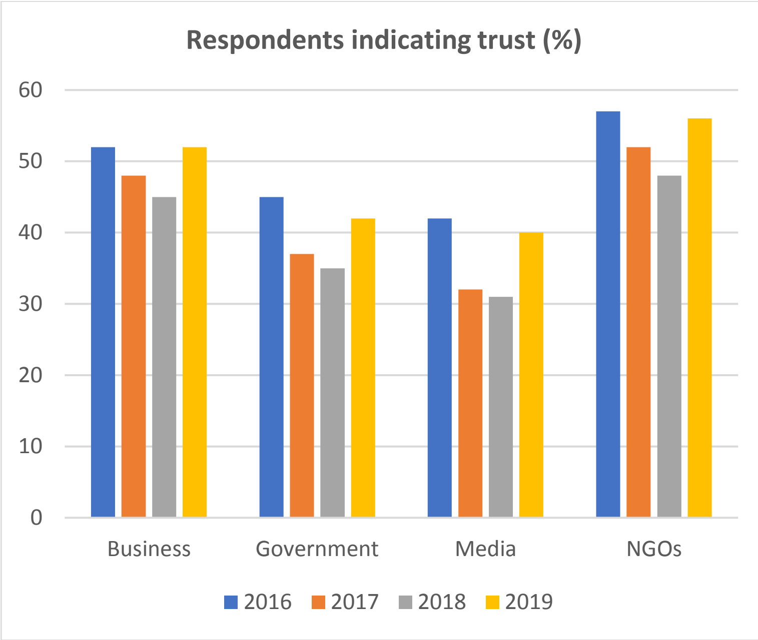
While diversification can present attractive opportunities to generate additional income to subsidise the core provision of social housing, the appraisal and management of the new and existing risks arising from this diversification is crucial.

Reputational risk

Although the recent 2019 annual Edelman trust barometer shows a slight rebound in trust compared with 2018, trust remains a significant issue for Australian institutions. The Edelman trust barometer provides a snapshot of citizen trust in various institutions through the dissemination of survey in 27 countries around the world.

Boards need to be aware that their actions will be scrutinised by a wide range of different stakeholders with a range of different perspectives, including tenants, lenders and investors, federal state and local governments, and the media.

Registered providers should ensure that they manage their business and manage their risks in such a way that they have regard to stakeholders' expectations in their decision making and do not damage the reputation of the sector as a whole. Retaining the trust and confidence of key stakeholders is key to providers achieving their own objectives.



Source: Edelman Trust

Beyond the missed opportunity and potential cost, failure to consider social and environmental outcomes in decision making can create risks or lead to incomplete decisions and the erosion of trust from communities and stakeholders.

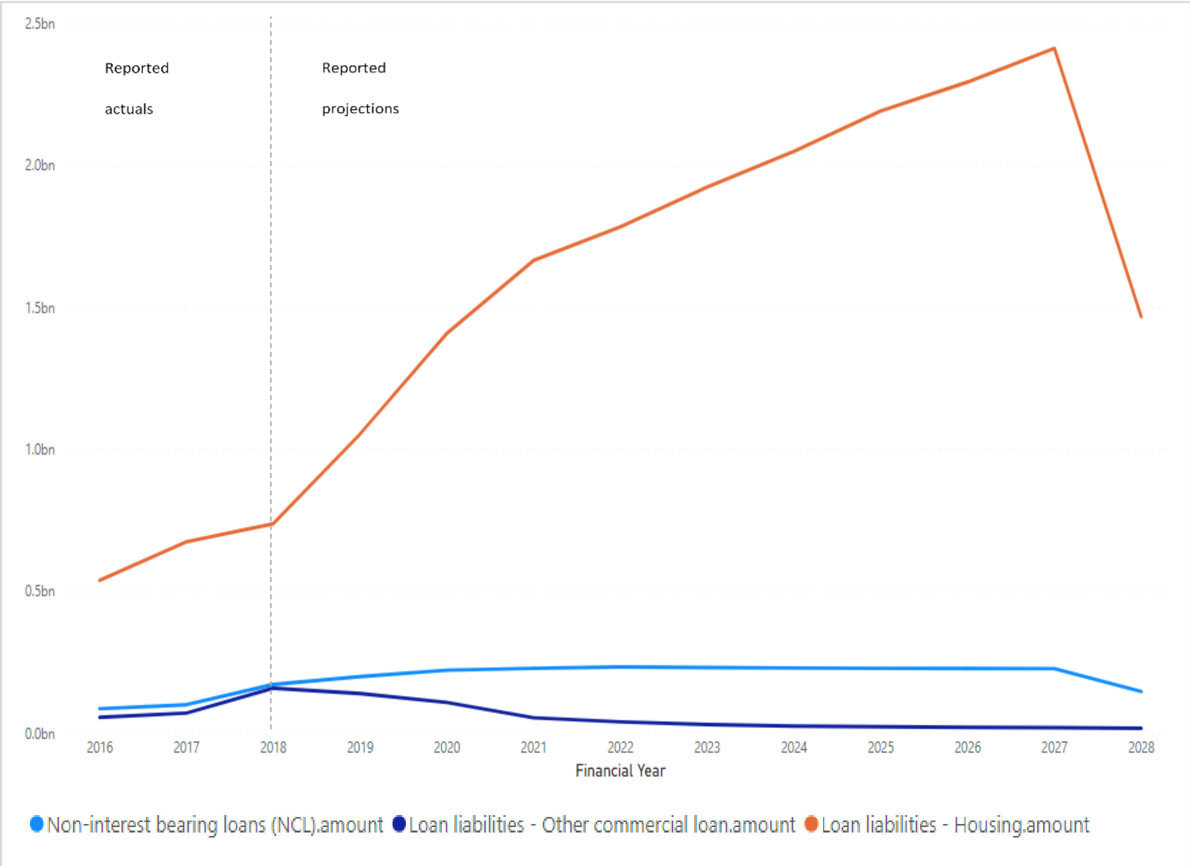
Funding trends

Effective financial governance is becoming increasingly important for registered CHPs across the sectors, as providers develop different relationships with a greater number of funders.

While sales revenue is becoming increasingly important for the financial viability of the sector, and is forecast to become more so, the sector is also expected to become increasingly reliant on longer-term debt from both government and private financiers.

As exposure to interest bearing debt increases, and providers look to new and diverse funding sources, it is important for registered providers to have precautionary measures in place that enable them to protect and withstand extreme and unexpected shocks to their business. Effective financial governance is therefore essential.

Actual and projected loan liabilities – NRSCH lodgements



NHFIC

The commencement of lending by the National Housing Finance and Investment Corporation (NHFIC), a Commonwealth government owned corporation established mid-2018 to operate an Affordable Housing Bond Aggregator accessible only to registered CHPs and a National Housing Infrastructure Facility primarily aimed at increasing the supply of affordable housing, has seen some modest improvements to the cost of providers existing debt.

An initial $315 million bond issued by the NHFIC to fund its Affordable Housing Bond Aggregator (AHBA) lending in March 2019 was priced at 2.38 percent and a subsequent $315 million bond issue was priced at 2.07 percent. In both instances the issuance was four times oversubscribed- which signifies a high level of market interest in future bond issuances by NHFIC, and indicates that the future borrowing costs for NHFIC should remain close to that of the Australian Government.

The result saw 10 year interest only finance provided to the first group of provider borrowers fixed at below 3 percent.

Market expectations are that bond prices will remain subdued for some time, which means that the forward-looking financing environment for registered providers remains positive.

While the focus of the NHFIC to date has been on the establishment of its AHBA products, opportunities remain for providers either directly or as part of special purpose vehicles (SPVs) with private partners to access cheap infrastructure financing for affordable housing developments, including grant funding, through the NHIF.

Private bank finance

In Australia, borrowing rates for households and businesses, as well as banks' funding costs, are at historically low levels.

The RBA has indicated that the availability of credit for construction is very different across the states. It also differs across cities within states, and even across suburbs within cities. A large part of these differences reflect different population dynamics, particularly migration flows. In turn, that also reflects differences in employment and income as well as differences in the cost of housing.

APRA changes

Banks have largely completed their transition to their higher 'unquestionably strong' capital ratios. Banks' resilience would increase further with the introduction by the Australian Prudential Regulation Authority of a Loss Absorbing Capacity (LAC) regime, which will require banks to raise an additional 3 percentage points of capital by 2024.

APRA is consulting on revisions to the capital framework for authorised deposit-taking institutions (ADIs) to implement 'unquestionably strong' capital ratios and the Basel III reforms and some key sector stakeholders have contributed to the process[2].

[2] https://www.communityhousing.com.au/wp-content/uploads/2019/11/Joint-APRA-Submission-Revisions-to-the-Capital-Framework-for-Authorised-Deposit-Taking-Institutions.pdf?x33467

Emerging technology related issues

The advent of artificial intelligence, machine learning and their ability to directly interact with customers and data via the internet has created numerous possibilities to assist tenants, better inform day to day business decisions and predict future trends and risks. These trends have also brought several key issues for providers to consider and manage.

Data accuracy

It is important that providers ensure that their data is accurate, comprehensive, up to date and in an easily accessible format for the purposes for which it is required.

Data accuracy is an important factor in enabling providers to ensure that they are making business decisions on true information, as well as to comply with all of their regulatory requirements. Particularly as registered providers broaden their focus outside of social housing management, it is critical that management and boards are confident in their understanding of these new areas of risk.

Accurate data is also necessary to ensure good quality compliance returns. As indicated in the Data Recommendations Paper, Registrars are increasingly reliant on accurate data to inform their regulatory interactions with providers.

Providers should also be aware of the emerging focus of Government agencies and regulatory efforts at protecting businesses and consumers from data breaches.

Privacy

Providers subject to the Privacy Act 1988 should already be aware of, and have taken steps to comply with, the Notifiable Data Breaches (NDB) scheme which came into effect on 22 February 2018. The NDB scheme requires organisations and agencies with obligations under the Privacy Act to notify the Office of the Australian Information Commissioner (OAIC) and impacted individuals about ‘eligible data breaches’. A data breach is eligible if it is likely to result in serious harm to any of the individuals to whom the information relates.

Cyber resilience

The increasing sophistication of providers business systems necessitate greater exposure to information technology applications and platforms, and with it increasing exposure to cyber risks and cyber-attack.

Cyber risks are dynamic—they can evolve or adapt quickly to changing environments. It is important to appreciate the trends and challenges in the cyber environment that may produce new or different cyber risks.

As a key current and emerging risk, provider boards and management should be satisfied that cyber risks are adequately addressed by the risk management framework of the organisation. The corporate regulator, the Australian Securities and Investments Commission, has set out a range of key questions that an organisation’s board should be asking management to ensure that cyber risks are being appropriately identified, monitored and managed.
While many registered providers may not be directly regulated by ASIC, these resources provide valuable guidance for boards in this emerging area.

For more information access https://asic.gov.au/regulatory-resources/digital-transformation/cyber-resilience/

Open data, big data and data mapping

There has been a clear trend over the past decade for Australian governments to increasingly release non-sensitive data for use by the community, researchers and businesses.

As a result, there is more information than ever available for providers to utilise in identifying and assessing opportunities to future areas of interest for development. Dramatic recent improvements in data accessibility through Local, State, Territory and Commonwealth government websites are increasingly allowing for cost effective opportunities to build community profiles with maps, information and charts about residents, housing and housing markets.

These data sources, and networks like the Australian Urban Research Infrastructure Network, are also enabling commercial and academic research to provide better insights on demographics, economic activity, urban design, transport and housing.

While access to these sources can assist providers to better understand the communities in which their housing assets are situated, as well as inform future business decisions, transforming open data into strategic investment decisions still requires the input of qualified professionals. This is particularly true in the assessment, design, financing, construction and management of property. Due to the substantial investment (and therefore risk) involved in the development of new property, ensuring the accurate assessment of cost, design, location and risks upfront is critical to making an appropriate decision.