31 March 2021

The Hon. Dominic Perrottet, MP
Treasurer
52 Martin Place
Sydney NSW 2000

Via email: bran.black@treasurer.nsw.gov.au

UDIA NSW Pre-Budget 2021-22 Submission

Dear Treasurer,

The Urban Development Institute of Australia - NSW (UDIA) is the leading industry body representing the interests of the urban development sector and has over 500 member companies in NSW. UDIA NSW advocates for the creation of liveable, affordable, and connected smart cities.

As you are all too aware, the urban development sector in NSW is an essential industry that contributed 7.2% of the NSW economy pre-covid and supports around 135,000 jobs. We are an essential economic bridge to the post COVID-19 recovery. Our pre-budget submission (see attached) shows that both greenfield and apartment markets face significant challenges with a loss of between $28bn and $50bn of economic output in FY23, reduced housing affordability and the loss of between 50,000 and 90,000 jobs between now and early 2023.

Greenfield Housing Supply

The challenge in greenfield markets is the lack of developable land. For greenfield markets, other than land re-zoning, the major roadblock to development is not having the enabling infrastructure in place. Given the short amount of time available to fix the greenfield development pipeline, we need a short-term solution that buys us time for longer-term reforms to kick in. We believe that the best way to solve the problem is to create a new fund, Jobs and Affordability (JAffa) Program that is a hybrid of the Housing Acceleration Fund (HAF) and the Accelerated Infrastructure Fund (AIF) focused on enabling infrastructure. The fund would distribute grants in two ways:

1. Provide incentives for Councils to forward fund their enabling infrastructure by borrowing via TCorp. We recommend that the legislation required to facilitate this change, which was recommended by the Productivity Commissioner, be implemented as part of the June 2021 budget. We believe that grants up to the value of $100m over three years would help deliver around two thirds of the Council's existing enabling infrastructure projects, catalyse the spending of $1bn of infrastructure funding, deliver approximately 25,000 homes and support around 30,000 jobs per annum.

2. Provide direct funding for key road and water projects in a similar way as the HAF. Historically, the HAF has earmarked in the region of $100m per annum. We believe that this level of funding will need to continue with a total fund of $300m over three years, helping to deliver around 10,000 homes and support 12,000 jobs per annum.

Apartment Pipeline

At the peak of apartment completions (FY18) 42,000 dwellings were built in NSW, sustaining up to 94,000 jobs. The NSW apartment market is struggling with approvals down nearly 63% from the 2016 approval peak and commencements down 43% and falling. UDIA forecasts that based on the current trend, there will be between 15,000 and 27,000 apartments completed per annum in the next few years in NSW, a drop of up to two-thirds, resulting in job losses of between 34,000 and 59,000 compared to 2018.

Given the need to do something quickly, we believe that the best way to fix the apartment market in the short term is to find ways of converting existing apartment approvals into construction commencements is by tackling the financing problem and reducing pre-sales barriers. The Government should consider three options:

1. Provide loan guarantees in exchange for lower project pre-sales thresholds.

2. Reduce foreign investor surcharges on new build apartments, a move that we believe will stimulate the market and **increase NSW Government revenues**.

3. A $25,000 property tax loan scheme for apartments based on the Federal Government's Homebuilder program but targeted at apartments and repaid by apartment owners as part of their property tax bill.

Overall, we believe that these budget measures would deliver excellent value for money for taxpayers, play a significant role in securing the economic recovery and put downward pressure on housing affordability.

We would value a meeting to discuss our proposals with you and will contact your office to arrange.

Yours sincerely,

Steve Mann
Chief Executive
UDIA NSW

Attached:
UDIA NSW Pre-Budget 2021-22 Submission

UDIA NSW PRE-BUDGET 2021-22 SUBMISSION

Supporting housing as a key bridge to economic recovery in NSW

Executive Summary

The Urban Development Institute of Australia - NSW (UDIA) is the leading industry body representing the interests of the urban development sector and has over 500 member companies in NSW. UDIA NSW advocates for the creation of liveable, affordable, and connected smart cities.

The construction of new housing and apartments is a key part of the NSW economy, supporting approximately 135,000 jobs (39,000 direct and 96,000 indirect) in FY19. Before the pandemic, the NSW development industry made up 7.2% of the NSW economy.

Unfortunately, both the new greenfield and apartment housing markets face significant but very different issues that if not addressed could produce:

- A significant drag on the NSW economy with a loss of economic output of between $28bn and $50bn in FY23.
- A loss of between 50,000 and 90,000 jobs.
- A housing affordability crisis, especially once the borders re-open.

Urgent action needs to be taken quickly so the sector can play its part in providing a bridge to the post pandemic recovery of the NSW economy and support housing affordability.

Greenfield Housing Pipeline

Greenfield house sales are well ahead of lot releases and there is now minimal trading stock in NSW. The combination of a lack of newly re-zoned land and enabling infrastructure, means that developable land is rapidly running out across the state. If immediate action is not taken to fix the lack of greenfield developable land supply, then new greenfield dwelling construction will grind to a halt over the next couple of years.

We believe that the best way to solve the problem is to create a new fund as part of a wider Jobs and Affordability (JAffa) Program, a hybrid of the Housing Acceleration Fund (HAF) and the Accelerated Infrastructure Fund (AIF) focused on enabling infrastructure. The fund would distribute grants in two ways:

1. Provide incentives for Councils to forward fund their enabling infrastructure by borrowing via TCorp. We recommend that the legislation required to facilitate this change, which was recommended by the Productivity Commissioner, be implemented as part of the June 2021 budget. We believe that a grant program up to the value of $100m over three years and up to 10% of the cost of any one item of infrastructure would help deliver around two thirds of the Council's existing enabling infrastructure projects, catalyse the spending of $1b of infrastructure funding, deliver around 25,000 homes and support around 30,000 jobs per annum.

2. Provide direct funding for key road and water projects in a similar way as the HAF. Historically, the HAF has earmarked approximately $100m per annum. We believe that this level of funding will need to continue with a total fund of $300m over three years helping to deliver around 10,000 homes and protecting 12,000 jobs per annum.

Apartment Pipeline

At the peak (FY18) of apartment completions, 42,000 dwellings were built in NSW sustaining up to 94,000 jobs. The NSW apartment market is struggling with approvals down nearly 63% from the 2016 approval peak and commencements down 43% and falling. UDIA forecasts that, based on the current trend, there will be between 15,000 and 27,000 apartments completed per annum in the next few years in NSW, a drop of up to two-thirds, resulting in job losses of between 34,000 and 59,000 compared to 2018.

Given the need to do something quickly, we believe that the best way to fix the apartment market in the short term is to find ways of converting existing apartment approvals into construction projects by tackling the financing problem and reducing pre-sales barriers. The Government should consider three options:

1. Provide loan guarantees in exchange for lower project pre-sales thresholds.
2. Reduce foreign investor surcharges on new build apartments, a move that we believe will increase NSW Government revenues.
3. A $25,000 property tax loan scheme for apartments based on the Federal Government's Homebuilder program but targeted at apartments and repaid by apartment owners as part of their property tax when the reform is taken forward.

Successful short-term support for the housing development sector would deliver both the greenfield housing and the apartments that are needed over the next three to five years and provide time for significant structural changes to take effect, protecting tens of thousands of jobs and maintaining tens of billions of dollars of economic output.

Overall, we believe that these budget measures would deliver excellent value for money for taxpayers, play a significant role in securing the economic recovery and put downward pressure on housing affordability.

Introduction

The importance of the development and construction sectors to the economy was recognised by both the Federal and NSW Governments in 2020. The Federal Government delivered HomeBuilder, a grant scheme that provided eligible owner-occupiers (including first home buyers) with a grant of up to $25,000 to build a new home or substantially renovate an existing home. The NSW Government supported the industry through ongoing Stamp Duty discounts for first home buyers and the Planning System Acceleration Program that sought to cut red tape and fast-track planning processes to keep people in jobs and the construction industry moving throughout the pandemic.

The NSW economy will not return to normality until international borders are re-opened welcoming migrants, tourists and foreign students back to the state. In the meantime, it is imperative that we do not hinder key economic sectors - such as urban development - from acting as a bridge to the economic recovery, which is crucial in supporting the jobs and business activity that will carry the economy through the current challenging times.

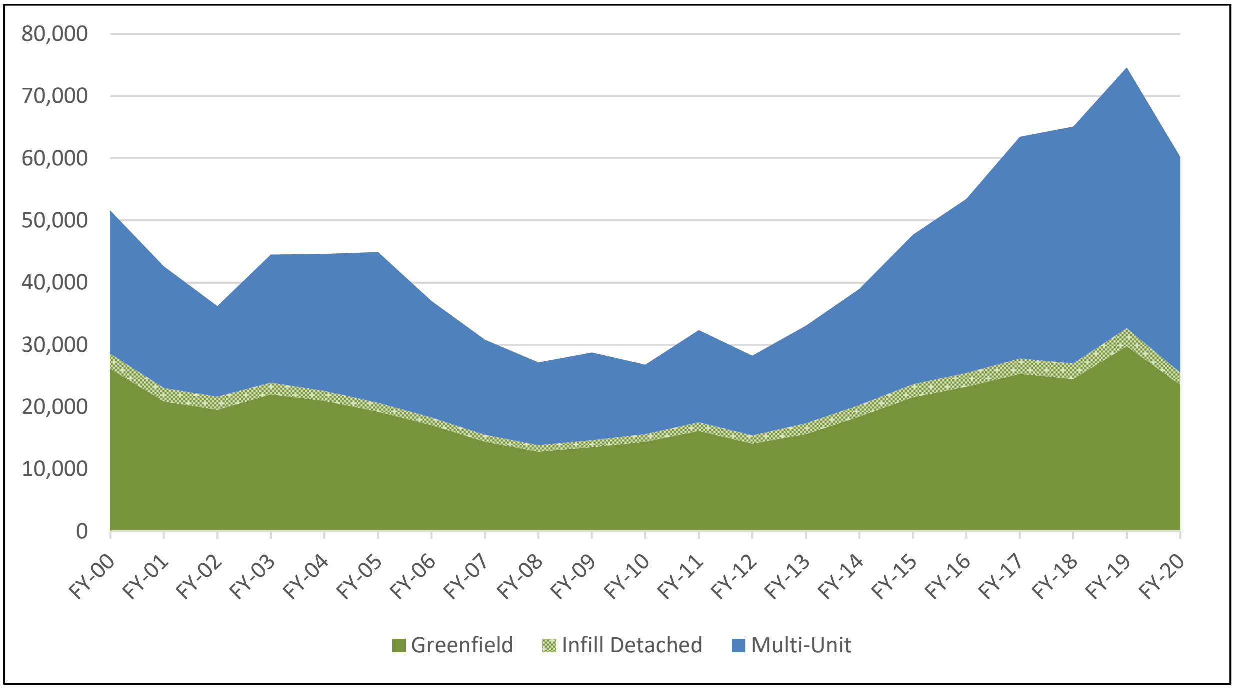
Unfortunately, both the new greenfield and apartment housing markets face challenging but very different issues that if not addressed, will see them become a major drag on the NSW economy and a source of significant job losses. We estimate that the loss of economic output in NSW will be between $28.4B and $50.7B and related job losses between **50,000 and 90,000** (14,000-25,000 direct).

UDIA's pre-budget submission to the NSW Government sets out below the challenges to both the greenfield and apartment markets and makes key recommendations for the 2021-22 Budget.

The Greenfield Housing Sector

In the last five years, on average around 25,000 greenfield dwellings have been built in NSW per annum, comprising 40% of the total new dwellings in NSW and supporting 60,000 jobs.

Annual Dwelling Completions by Type, New South Wales



Source: UDIA; DPIE; ABS

Historically, the sector has been provided with developable land through a combination of re-zonings and enabling infrastructure – water, sewerage, power and roads. Since 2011 and the end of the 'Sydney is full' mantra from the previous state government, the sector has been able to play an important role in the success of the NSW economy. However, the steady rate of re-zonings from 2011-2014 such as Austral-Leppington and Wilton in 2017, has now slowed down. As more greenfield dwellings have been constructed, the lack of re-zoning has steadily reduced the pipeline of re-zoned land available for development.

The NSW Government has long recognised that business as usual funding processes do not channel sufficient funds into enabling infrastructure for housing which led to the creation of the Housing Acceleration Fund (HAF) in 2012. HAF provides grants for critical infrastructure projects which help accelerate the delivery of housing. Projects funded under the HAF include transport, water, wastewater, drainage and community infrastructure. HAF has reserved over $1bn for more than 50 future projects in both regional and metropolitan areas.

In 2020, as part of the response to the pandemic, UDIA worked with the NSW Government to create the Accelerated Infrastructure Fund (AIF), part of the Planning System Acceleration Program. The AIF provided $75.9 million to support the delivery of community infrastructure in the high growth areas of Blacktown and The Hills Local Government Areas (LGAs) in North West Sydney. This included funding for councils to deliver local roads, stormwater infrastructure and public open space projects to unlock plans for development of new homes and employment land. The objectives of the fund were to:

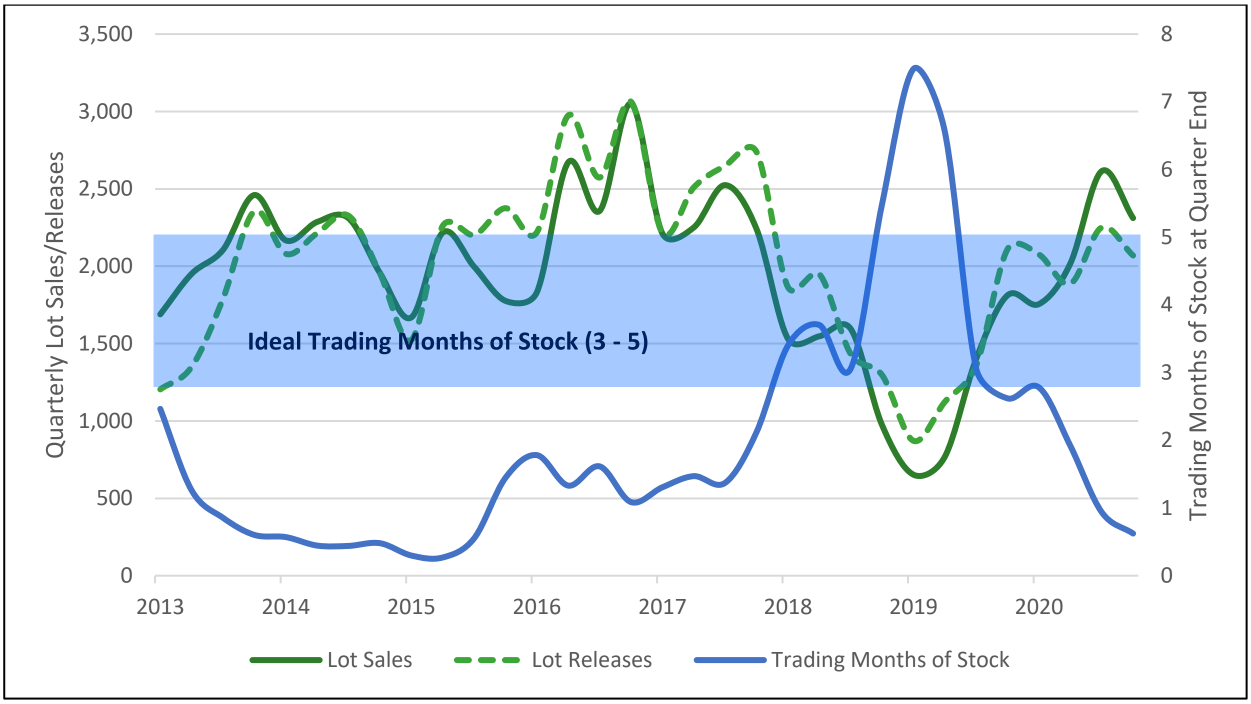
1. Fund infrastructure that unblocks development approvals and enables development activity;
2. Stimulate construction activity by investing in 'shovel-ready' infrastructure projects;
3. Reduce local developer contributions; and
4. Encourage developers to enact development approvals and invest in construction.

The AIF funds provided by the State Government were matched by the Councils delivering a double dividend, supporting enabling infrastructure projects worth $146m, the development of thousands of new homes and 1000 new jobs during construction.

For many years, urban development has contributed to the costs of infrastructure through various forms of infrastructure contributions. UDIA has long advocated for a review of the current infrastructure contributions system which is widely recognised as broken. This led to the NSW Productivity Commissioner making 29 recommendations in 2020 to help fix the system, all of which have been accepted by the NSW Government and infrastructure contributions reform is now underway. If successful, this will help to deliver infrastructure to support greenfield development in a timelier manner. However, in the short term, the existing regime will apply and even when implemented, the full benefits of the reforms will take years to be realised.

As has been widely reported, the greenfield housing sector is currently seeing strong growth with land sales in Greater Sydney up 88% in 2020, thanks to low interest rates, the HomeBuilder stimulus scheme, the desire for increased living space due to COVID-19 and the greater need for, and acceptance of working from home.

Quarterly Greenfield Housing Activity, Greater Sydney



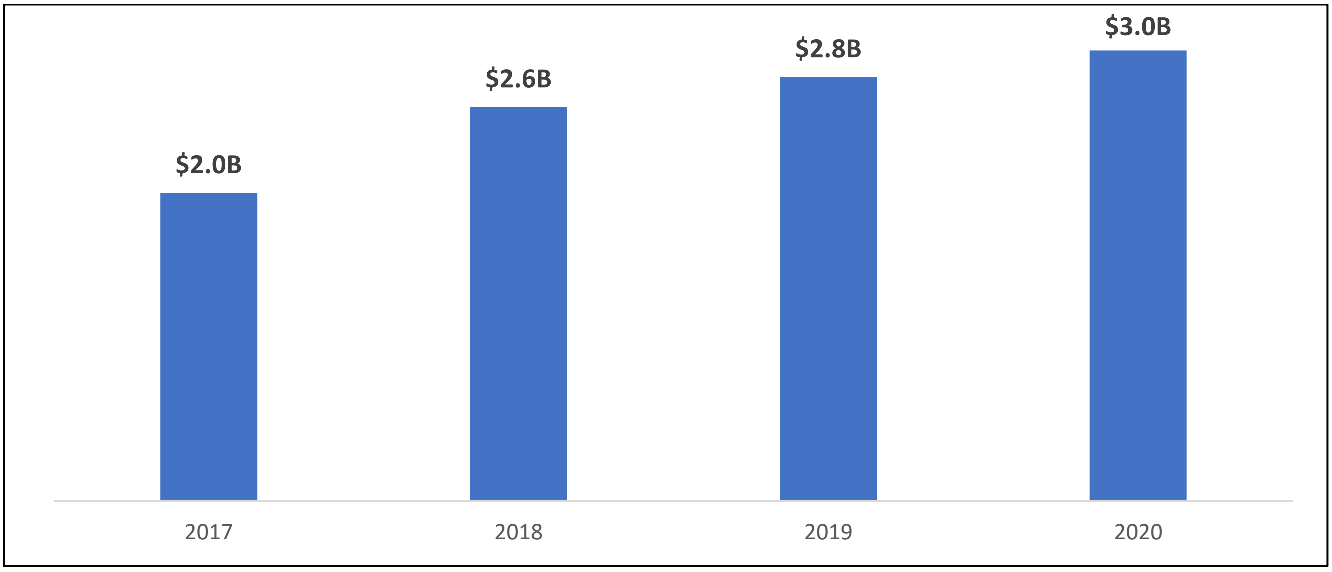
Source: UDIA; Research4

It is easy for this success to breed a sense of complacency. However, the chart above shows sales well ahead of lot releases and minimal trading stock. It does not require a crystal ball to see that trouble lies ahead. The combination of a lack of newly re-zoned land and enabling infrastructure, means that developable land is rapidly running out across the state.

If immediate action is not taken to fix the lack of greenfield developable land supply, then new greenfield dwelling construction will grind to a halt over the next couple of years, causing increasing pressure on housing affordability, the loss of between 17,000 and 30,000 jobs and placing a significant dent in the post pandemic economic recovery in NSW.

Research by the UDIA has found that Councils in the Sydney Mega Region (Illawarra to the Hunter) were sitting on almost $3bn at the end of FY20 (up 6.8% from FY19) in infrastructure contributions, up from $2bn four years ago. UDIA has estimated that over $550m is earmarked for enabling infrastructure, that if delivered could help unblock the greenfield supply pipeline. Unfortunately, under the current system, Councils are spending significantly less than they obtain from infrastructure contributions with only 18% of Councils total holdings spent in FY20 (see chart below).

Contributions Held by Councils



Source: UDIA; Local Council Annual Reports

Enabling infrastructure is failing to keep up with the needs for development for a number of reasons including:

1. **Prioritisation process -**The standard NSW Government processes for prioritising infrastructure do not adequately account for the needs of the broader economy. For example, in the case of Transport for NSW (TfNSW), new transport projects rightly need to have a viable business case with a Benefit Cost Ratio (BCR) above 1.0. However, the agency does not sufficiently prioritise projects based on the size of the BCR, prioritising projects that provide significant transport benefits, but failing to invest sufficiently in projects that deliver significant land use benefits. The HAF was partially designed as a 'band-aid' to deal with this problem.

2. **IPART Processes**. Water infrastructure providers are required to get their investments approved by IPART. Unfortunately, these processes are considered by many to be extremely conservative, to the point where providers find it very difficult to make the case for forward funding of infrastructure to support new housing. This results in a very inflexible system and long delays to housing development.

3. **Timeliness to fully fund Infrastructure.** Infrastructure contributions collected by Councils for pieces of infrastructure can take years to become fully funded. Unfortunately, until they are fully funded, under the current infrastructure contributions systems, it is very difficult for Councils to deliver infrastructure. Again, the inflexibility of the system results in long delays to housing development.

4. **Lack of co-ordination**. Historically, transport, infrastructure and land use plans have not been integrated, resulting in disjointed projects. Although at a strategic level this situation has improved, the reality on the ground has barely changed.

5. **Lack of enabling infrastructure identification**. In many parts of the state, there has not been a program for identifying and co-ordinating enabling infrastructure. In 2020, UDIA led a pilot scheme, the Urban Development Program (UDP), in South-West Sydney to tackle these issues. UDPs now need to be established where they do not currently exist such as Greater Sydney.

Greenfield Housing Solutions

To properly fix the greenfield pipeline problem will require significant structural reforms including those already being undertaken such as infrastructure contributions, as well as those that are needed but are not yet on the Government's agenda.

Unfortunately, there is not time for these structural reforms to be undertaken and their impact to be felt to avoid the greenfield development bottleneck. Action needs to be taken now to avoid major problems occurring in the next couple of years. In developing solutions to these problems, UDIA has followed three principles:

1) Fix the short-term problem, enabling housing delivery over the next three years.
2) Provide value for money for NSW taxpayers.
3) Invest in projects that provide both short and long-term benefits.

We believe that the best way to solve the problem is to create a new fund as part of a wider Jobs and Affordability (JAffa) Program that is a hybrid of the HAF and AIF and is focused on enabling infrastructure. The fund would distribute grants in two ways:

1. Provide incentives for Councils to forward fund their enabling infrastructure, utilising the infrastructure contributions they are already collecting. The Productivity Commissioner has recommended making it easier for Councils to borrow via TCorp and this has been accepted by the Government. We recommend that the legislation required to facilitate this change be implemented as part of the 2021/22 budget. At the same time, to motivate Councils to make use of the facility and create momentum, the NSW Government should provide a Council grants program for specific pieces of enabling infrastructure for the final 10% of the cost of infrastructure. We believe that a total grant fund up to the value of $100m over three years would help deliver around two thirds of the Council's existing enabling infrastructure projects, catalysing the spending of $1bn of infrastructure funding. Even if we assume a very high cost per dwelling of $40,000 this would deliver approximately 25,000 homes and support around 30,000 jobs (8,000, direct and 22,000 indirect). For example, the Regent Street Detention basin and Boundary Street Bio basin in Blacktown will unlock 3,500 dwellings at a cost of $27m.

2. Provide funding for key road and water projects like the HAF. Historically, the HAF has earmarked in the region of $100m per annum. We believe that this level of funding will need to continue with a total fund of $300m over three years helping to deliver around 10,000 homes and protecting 12,000 jobs per year. For example, an upgrade to Moss Vale Road and intersections will unlock 4,000 homes at a cost of $30m.

The JAffa program should be established to help solve the historic lack of infrastructure co-ordination. Many greenfield housing developments require roads and water infrastructure to enable housing delivery. The program needs to assess the benefits of pieces of infrastructure wholistically and not in isolation.

Recommendation 1 – *Amend the legislation to make it easier for Councils to borrow from TCorp and provide financial incentives for Councils to begin using the facility to deliver enabling infrastructure.*

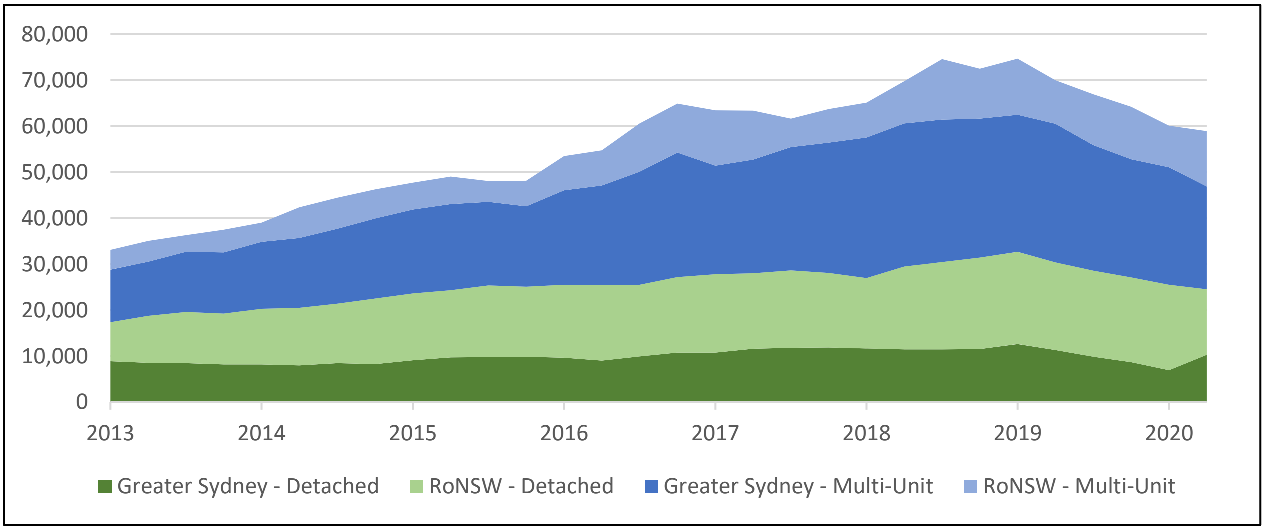
Recommendation 2 – *Provide direct funds (similar to the HAF) for enabling infrastructure.*

Recommendation 3 – *Co-ordinate enabling infrastructure delivery to facilitate housing supply.*

The Apartments Sector

At the peak (FY18) of apartment completions, 42,000 dwellings were built in NSW sustaining up to 94,000 jobs (27,000 direct and 67,000 indirect). Apartments have become the mainstay for new housing supply in NSW, moving above 50% over the last 6 years and just below 60% in 2018.

Rolling Annual Dwelling Completions in NSW by region and type



Source: UDIA; DPIE

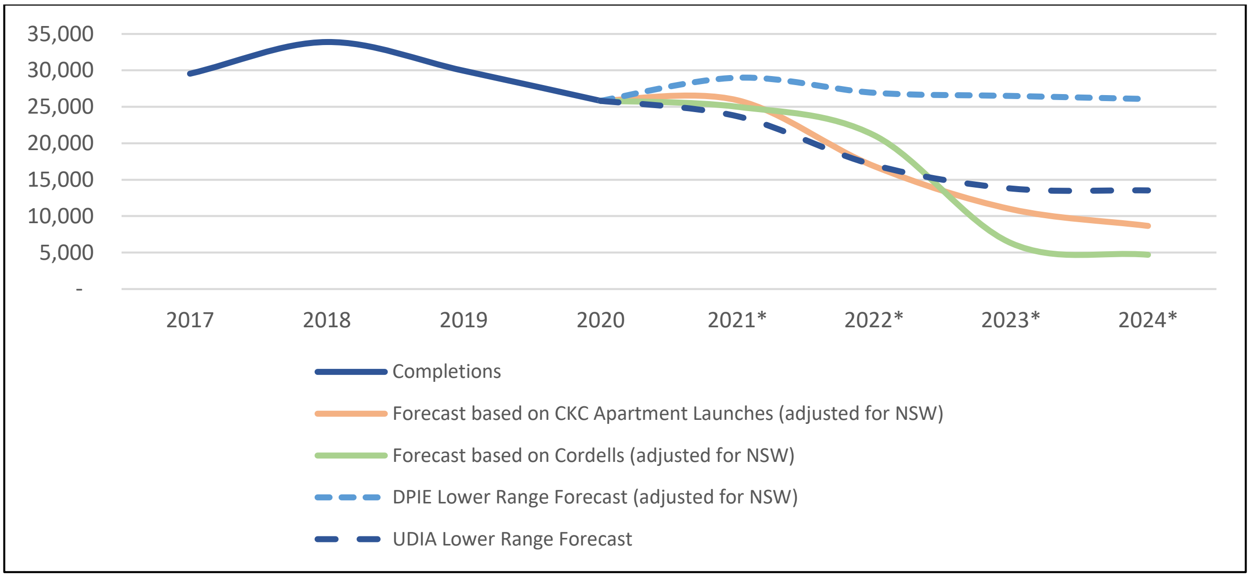
Apartments in NSW are mostly delivered by small and medium sized developers, representing 66% new apartments over the last three years.

The common financing model for apartment development has been to obtain planning permission and then sell off-the-plan apartments before construction commenced. These 'pre-sales' provided the banks with the confidence to lend to small and medium sized developers. Pre-sales were boosted by a combination of purchases by recent immigrants, overseas students and foreign investors.

Planning permission is often dependent upon the creation of viable precinct plans. Unfortunately, the precinct plans process has had many challenges, with priority precincts even dating back to 2014, still not completed.

Although it is not widely reported in the press, the NSW apartment market is struggling with approvals down nearly 63% from the 2016 approval peak and commencements down 43% and falling. UDIA forecasts that, based on the current trend, there will be between 15,000 and 27,000 apartments completed per annum in the next few years in NSW see chart below), a drop of up to two-thirds, resulting in job losses of between 34,000 and 59,000 compared to 2018.

Annual Apartment Completions Forecasts, New South Wales



Source: UDIA; ABS; DPIE; Charter Keck Cramer; CoreLogic

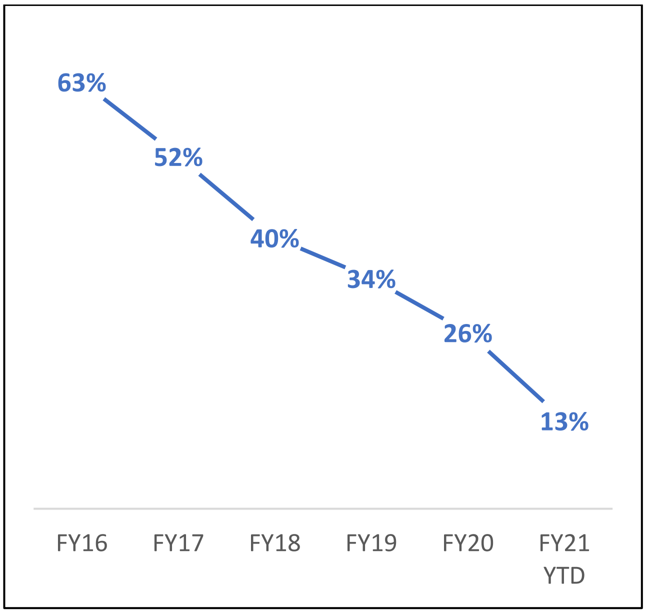
The current challenges in the apartment market have been caused by a number of factors including:

- Taxes on foreign investment;
- Prudential changes for loans to investors;
- Pandemic related reductions to immigration and student numbers;
- Apartment construction scandals;
- Pandemic related uncertainty; and
- Lack of clarity re SIC's, PIC's, and uncapped Council charges.

All of these factors have combined to make it very difficult to obtain pre-sales and therefore finance for apartment projects. According to Urbis' *Apartment Essentials*, there are currently 8,450 apartments in the 'pre-sales' stage of development in Greater Sydney and there are a further 38,480 apartments in projects which have approvals and could move to pre-sales.

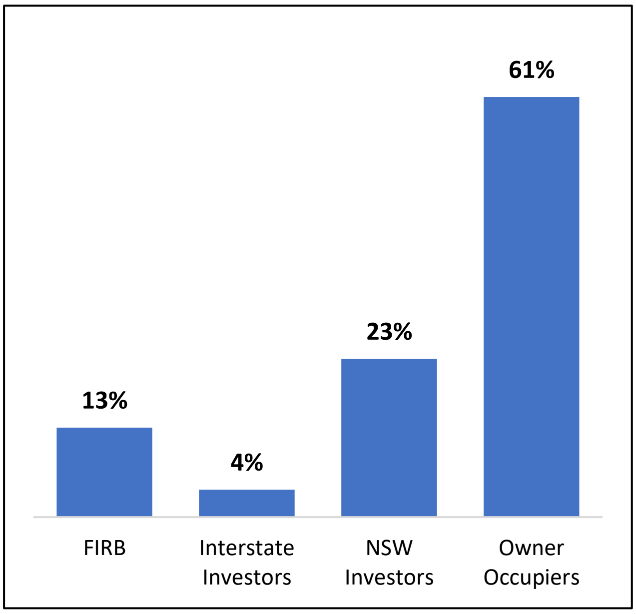
Since the foreign investor surcharge purchaser duty was introduced in 2016, there has been a dramatic decrease in foreign investment into new apartments:

UDIA Member Foreign Investor Proportion of Sales



Source: UDIA

New Apartment Purchaser Segments, Sydney



Source: Urbis Apartment Essentials, Q4-2020

Obviously, the pandemic and the resulting closure of international borders has hit the apartment market hard. Therefore, any self-sustaining recovery will be dependent upon the borders re-opening. Most people do not believe that this will occur in 2021 and that the chances of opening up in 2022 will depend greatly on factors outside the control of the Australian Government including the pace of the vaccination rollout globally and the continuing global spread of the virus.

Despite the myriad problems in the apartment market, it is easy to be complacent and leave it to pick up when the borders re-open. This is a myopic view with two significant negative consequences:

1. **Affordability -** Servicing work for approved new greenfield lots and construction of a house can typically be completed in 12 to 18 months. However, apartments take at least double that time to reach completion once pre-sales and financing have been obtained. We need projects commencing now for 2023 and 2024 completions. Once the borders re-open, the current stock of apartments will be rapidly occupied (with vacancy currently sitting at 4%) leaving a long gap before new stock comes on stream. This will put significant pressure on affordability for first time buyers who often choose an apartment as their first rung on the property ladder.

2. **Job losses –** As mentioned above, given the current state of the apartment market, significant skilled job losses are likely to occur if things do not turn around soon. This will also create the challenge of losing a skilled workforce that will take years to replace, reducing the capacity of the sector to produce the required supply when borders do re-open and demand does bounce back.

The Government's proposed move to a Property Tax, by enabling buyers to opt out of paying Stamp Duty, has the potential to provide some stimulus to the apartment market. However, we do not believe that this will have a major effect on pre-sales.

Apartment Supply Solutions

To properly fix apartment market supply will require structural reforms to the precinct and DA processes. However, these are not currently being taken forward and, given the need to do something quickly, we believe that the best way to fix the apartment market in the short term is to find ways of converting existing apartment approvals into construction projects by tackling the financing problem and reducing pre-sales barriers. The Government should consider three options as part of its JAffa program:

1. **Provide loan guarantees in exchange for lower project pre-sales thresholds**. Governments around the world including NSW regularly provide loan guarantee schemes. Indeed, as part of the response to the pandemic, the NSW Government provided up to $750m via a loan guarantee scheme to help universities through the COVID-19 pandemic. We believe that an equivalent scheme for apartments could play a significant role in getting construction moving. Given the bounce back that will come in the apartment market when borders re-open, this should prove to be a sound investment by the NSW Government.

2. **Reduce foreign investor surcharges on new build apartments.** Given the current lack of pre-sales in the new build apartment market, the revenues that the Government will obtain from the surcharge in the forward estimates is going to be minimal. We believe that a significant cut in the surcharge for new apartments only could provide a significant boost to activity and **increase the revenues obtained by the NSW Government**. For example, a halving of the surcharge would need a doubling of apartment sales to maintain revenue neutrality. Given investors make up just 13% of the very low levels of activity in the apartment market currently, doubling activity would be an achievable but effective goal.

3. **Property tax loan scheme for apartments -** The Federal Government's HomeBuilder scheme has been extremely successful at boosting greenfield housing markets. A similar scheme, but one that is adapted for the apartment market and repaid via the property tax, has the potential to significantly boost pre-sales, enabling more apartment construction.

   A stimulus of $25,000 for apartments could support 10,000 pre-sales at a total cost of $250m and enable the financing of 20,000 apartments. However, if this stimulus was structured to support the proposed property tax, it could be added to the annual property tax bill until the stimulus was re-paid by the property owner, making the stimulus effectively a loan.

Any stimulus should only be available to properties from 'Trusted Developers', as defined by the NSW Building Commissioner, to ensure quality and the developers must commit to construction commencement within 12 months.

These three options for apartments are not mutually exclusive and could be undertaken together.

Recommendation 4 – *investigate three mechanisms for supporting the apartment market until international borders re-open including providing loan guarantees, reducing foreign investor surcharges on new build apartments and a property tax loan scheme for apartments.*

Conclusion

If no action is taken, the challenges in both the apartment and greenfield housing development markets could:

- Produce a significant drag on the NSW economy with a loss of economic output of between $28bn and $50bn in FY23.
- A loss of between 50,000 and 90,000 jobs.
- A housing affordability crisis, especially once the borders re-open.

Urgent action needs to be taken quickly so the sector can play its part in providing a bridge to the post pandemic recovery of the NSW economy and support housing affordability.

As part of this year's budget, the NSW Government should undertake a Jobs and AFFordAbility (JAffa) program. The program should support enabling infrastructure delivery for the greenfield sector and pre-sales activity in the apartment market. This will help to deliver 37,500 greenfield homes over three years, unblock thousands of apartments and support tens of thousands of jobs.

A successful program would deliver both the greenfield housing and the apartments that are needed over the next three to five years and provide time for significant structural changes that are underway and designed to deliver greater productivity in the planning system, such as infrastructure contributions reform, to take effect. The program also aligns with the NSW Government's proposed Property Tax reforms.

Over the next couple of months, UDIA will be undertaking a deeper analysis of the enabling projects that need to be taken forward to inform the Government and ensure continued greenfield housing supply.