



Kāinga Ora-Homes and Communities and Ministry of Housing and Urban Development Report: *Review of Current Funding and Financing Arrangements*

Reference number	BN 19 038 BRF19/20110505
Date	26 November 2019
Priority	Normal
Security level	In confidence

Action sought

Recipient	Action sought	Deadline
Minister of Housing	<p>Forward a copy of this report to the Minister for Finance</p> <p>Agree to discuss with the Minister of Finance an increase in the private debt facility for Kāinga Ora to \$7.1 billion to enable the organisation to deliver on short-term commitments and maintain momentum</p>	Decisions on Kāinga Ora's debt limit are required by December to enable it to deliver on short-term commitments and maintain momentum.

Contact for discussion (if required)

Name	Position	DDI Mobile	Email	First contact
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For Minister's Office

☐ Noted ☐ Approved ☐ Not approved ☐ Other

Comments

26 November 2019

Minister of Housing

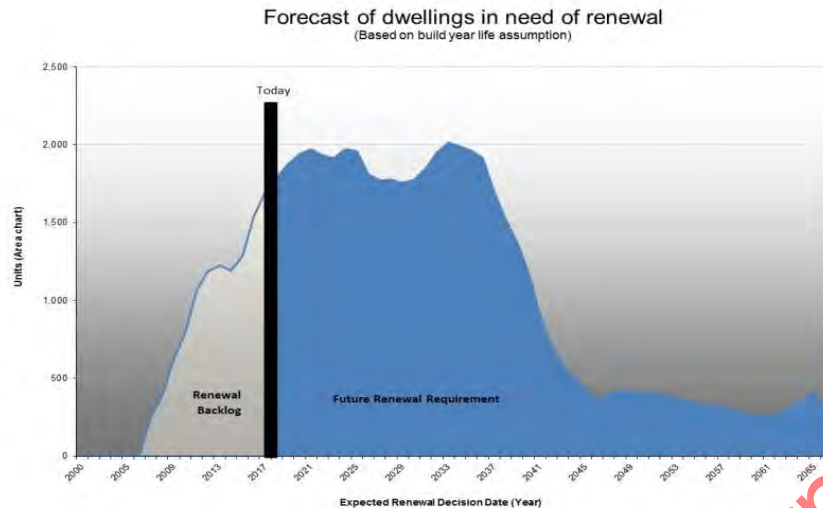
Review of Current Funding and Financing Arrangements

Executive summary

- 1 This briefing is the first of two agreed reports back [BRF 19/20090412]. It provides you with advice on short term options to maintain momentum on Kāinga Ora's existing work programme in order to deliver Government priorities while minimising whole of government costs and staying within prudent borrowing limits. The briefing sets out financing options, including increasing the existing debt ceiling. It also provides advice on new initiatives agreed by Ministers where decisions on financing are needed to be made now or imminently and decisions for Budget 2020.
- 2 Based on latest information Kāinga Ora's four-year capital programme is expected to deliver (amongst other things):
 - Compliance with Healthy Homes legislation (interventions in circa 60,000 homes over four years)
 - The complex remediation programme (over 500 units)
 - 1,500 – 2,200 homes brought to a modern standard and fit for purpose for another 50 years through the retrofit programme
 - 4,480 additional IRRS homes plus another 1,200 homes in FY23 and replacement of homes to support growth
 - Disposal of 400 surplus and high value homes over the next four years
 - Stage 1 Transitional homes, 360 more homes to support refugee housing, up to 115 homes for corrections to assist reintegration of prisoners into communities, provision of more community group houses
 - Financing of the Tamaki regeneration
 - Progressing the Northcote, Mangere, Mt Roskill and Oranga urban development programmes delivering improved master planned communities, developed sites for new state housing and super-lots for sale for market/affordable homes
 - Delivery of around 700 transitional homes this year to help permanently end reliance on motels (PERM)
 - Continuance of this objective through Kāinga Ora delivering an additional 1,000 transitional homes in FY21 and 1,200 in FY22¹

¹ While the Government has agreed to only the first year of PERM, as part of developing its future pipeline Kāinga Ora is seeking financing capacity in anticipation of further places being sought, whether as transitional housing or public housing. Funding these additional places will be determined through Budget 2020.

- Provisions for new land development activities to support housing supply and affordability by Kāinga Ora
 - Contingencies to provide coverage for further price escalation, unanticipated ground conditions and infrastructure requirements and erosion of sales revenues
- 3 This spend will result in significant savings elsewhere to the Crown and will (in line with Kāinga Ora's operating principles set out in the legislation) contribute to the social, economic, environmental, and cultural well-being of current and future generations by:
- Providing public housing solutions that contribute positively to well-being including
 - providing good quality, warm, dry, and healthy rental housing; supporting tenants to be well connected to their communities; and to lead lives with dignity and the greatest degree of independence possible; and to sustain tenancies
 - working with community providers to support tenants and ensure those most in need are supported and housed
 - being a fair and reasonable landlord, treating tenants and their neighbours with respect, integrity, and honesty
 - *Providing housing supply that meets needs by*
 - managing its housing stock prudently, including upgrading and managing its housing to ensure it remains fit for purpose
 - ensuring that the housing it develops is appropriately mixed (with public, affordable, and market housing) and is of good quality
 - *Supporting the development of well-functioning urban environments by*
 - ensuring its urban development contains quality infrastructure and amenities that support community needs
 - assisting communities where it has housing stock to develop and thrive as cohesive and safe places to live
- 4 Appendix 1 summarises the anticipated benefits to Kāinga Ora's customers, the Crown and Kāinga Ora that are expected to be realised as a result of this.
- 5 Kāinga Ora's current funding and financing model involves it:
- Meeting core operating expenditure (tenancy management and maintenance) through rental revenue, which results in an operating surplus (free cashflows) of ~\$380m per annum
 - Meeting capital programme costs upfront through borrowing, which is serviced through these operating surpluses, operating supplements and sales
 - Preparing business cases to ensure there is enough funding to service debt before undertaking capital investment and raising debt.
 - Raising debt to address a peak period of asset renewal (as shown below) over the next twenty years. This debt can then be repaid over the subsequent years, when maintenance and renewal requirements are much lower.



- 6 A summary of Kāinga Ora's sources and uses of funds over four years is provided in Appendix 2.
- 7 Kāinga Ora currently has a borrowing protocol limit of \$3.7 billion. This is made up of:
 - the debt required to meet its obligations for the four years ending June 2022 as at June 2018 (\$3.05 billion). This included delivery of the 4,480 new public housing places announced in Budget 2018, and advancing the Auckland Housing Programme projects at Māngere, Mt Roskill, Oranga and Northcote.
 - \$650 million agreed with the Minister of Finance to increase Kāinga Ora's private debt limit in November 2019 to enable the delivery of transitional places (between CHPs and Kāinga Ora) this financial year and begin work on the FY21 and FY22 programme;
- 8 Kāinga Ora signalled in April this year that its debt limit was not enough to allow it to deliver its four-year budget intentions. This is due to a range of underlying factors including new activities, scope changes, unforeseen events, changing market conditions, delayed realisation of scale and innovation efficiencies, and changes to dwellings mixes, delivery timeframes and yields. This has resulted in costs being higher than budgeted (notably for land remediation, construction and infrastructure) and revenues lower than anticipated (due to an unanticipated drop in land values and increased levels of affordable housing).
- 9 In effect while initial business cases signalled land sales would support new activity such as housing affordability and urban renewal higher than anticipated costs and lower revenues mean this activity is now relying on operating surpluses. Over time Kāinga Ora projects there is still sufficient surpluses to meet its investment plans, however, a funding source for urban development and affordable housing activity will need to be identified to scale this up over time.
- 10 Kāinga Ora now expects to reach its private debt cap by mid-2020 meaning it will no longer be able to sign new contracts from around February 2020 (essentially a contracted breach i.e. Kāinga Ora will need to contract delivery in advance to paying for delivery).
- 11 To deliver Kāinga Ora's future investment intentions to June 2023 it will need approximately \$10.7 billion:
 - \$8.7 billion in debt or equity injections to meet revised budget intentions, including new approved initiatives, cost increases and scope changes, and

- \$2 billion to additionally meet planned activity which consists of:
 - \$1.7 billion under the PERM initiative (of which \$650m has already been approved)
 - \$0.25 billion to provide provisions for new land development initiatives
- 12 In order to give Kāinga Ora headroom to continue to deliver upon current commitments and the first two years of the PERM work it is recommended that interim approval be given for Kāinga Ora's debt limit to be raised to \$7.1 billion. This would enable Kāinga Ora to deliver on its budget intentions to June 2021, support the delivery of the first two years of PERM, sign some contracts for 2022 onwards and have provisions for new land development activities, noting that Kāinga Ora and HUD will come back to you in June 2020 with a more comprehensive, longer term view of funding and financing requirements for the organisation. This paper however is only seeking an interim increase to the debt protocol.
- 13 Approval of an increased debt limit would enable Kāinga Ora to transact decisions up to an agreed amount. Agreement to a limit would not provide approval for investment decisions. Investment decisions are and will continue to be made through detailed Programme Business Case disciplines which provide for a consultation process with the Kāinga Ora Board and yourself where these are over agreed thresholds.
- 14 It is important to also note that the Crown largely determines the drawdown of this debt through its funding decisions i.e. if IRRS were limited Kāinga Ora would not grow its portfolio.
- 15 At this stage this increased debt does not require additional funding however as noted in paragraph nine additional new activity will make this necessary.
- 16 It is proposed the June 2020 report will build on the decisions sought in this paper around the short-term funding and financing requirements for Kāinga Ora's current project pipeline by taking a broader view on how Kāinga Ora can best be enabled to deliver with partners on the wider outcomes sought for the Housing and Urban Development system. This policy advice will:
 - Confirm the outcomes sought for the system and how the known pipeline of projects will be prioritised to deliver them;
 - Separately and transparently set medium to long term objectives and funding levels for each of the main areas of activity for Kāinga Ora;
 - Agree a prudent and sustainable debt profile through time and other associated funding requirements; and
 - Integrate the funding and financing model for Kāinga Ora with other workstreams underway such as the Public Housing Funding Review and Procurement Plan.
- 17 In addition, we will report on a comprehensive review of the large-scale programmes.
- 18 Without an interim extension of its debt limit, Kāinga Ora will need to put current programmes on hold as early as February 2020. It has taken Kāinga Ora years to achieve the scale and pace it is currently delivering, regaining lost momentum would take time and likely cost it more.
- 19 We recommend that you forward a copy of this report to the Minister for Finance. We will consult with Treasury and your office about the timing of a bilateral meeting

with the Minister of Finance. Subject to the outcome any discussions with the Minister of Finance, we will prepare an Approval Document for the increase in the debt protocol, and a Cabinet Paper if you wish to consult Cabinet.

20 We would welcome discussion with you on any of the points raised in this paper.

Recommendations

We recommend that you:

- a. **Note** that in September 2019 you agreed to a two-stage review of funding and financing arrangements for Kāinga Ora comprising:
 - i. advice on options for the existing work programme in order to deliver Government priorities while minimising whole of government costs and staying within prudent borrowing limits, for Ministers to make decisions by 30 November 2019; and
 - ii. a more comprehensive review of the medium-long term funding and financing model for Kāinga Ora to enable Ministerial decisions by June 2020;
- b. **Note** that the advice in this briefing considers options to address funding and financing shortfalls associated with the following existing plans or commitments:
 - i. firm commitments within current funding and financing (core business as usual and legislative and contracted projects);
 - ii. commitments announced by Ministers that were adequately funded and financed, but costs and/or anticipated revenue have shifted; and
 - iii. plans endorsed by the HNZ Board, including those without funding;
- c. **Note** that announcements by Ministers around Porirua East are currently not funded, however a tagged contingency for Porirua East is being sought through Budget 2020 for supporting infrastructure to enable the first neighbourhood redevelopment.
- d. **Note** that Kāinga Ora has inherited Housing New Zealand's funding and financing model, made up of:
 - i. operating funding (including the Income Related Rents Subsidy and other appropriated funding sources);
 - ii. selling surplus land; and
 - iii. borrowing (from both the private sector and the Crown).
- e. **Note** that Ministers and Cabinet make decisions on the level of debt Kāinga Ora should manage, the extent of growth of public housing, and elements of operating funding;
- f. **Note** that Cabinet established a private debt limit for Kāinga Ora of \$3.05 billion;
- g. **Note** that the debt limit of \$3.05 billion was expected to finance the Long-Term Investment Plan of Kāinga Ora up to 30 June 2022, including delivery of the 4,480 new Kāinga Ora public housing places announced in Budget 2018; and advancing

the Auckland Housing Programme projects at Māngere, Mt Roskill, Oranga and Northcote;

- h. **Note** that Kāinga Ora cannot deliver the range of existing commitments within its agreed debt limit, due to a range of factors, including new commitments, increases in scope, growth of public housing requirements, costs being higher and revenues lower than anticipated;
- i. **Note** Kāinga Ora expects to reach its private debt limit by June 2020 (excluding new investment related to homelessness), and that Kāinga Ora needs to enter into contracts ahead of actual spend, and it is anticipated that it will not be able to sign new contracts from February 2020 without leading to a breach in the debt limit post June 2020;
- j. **Note** you have previously agreed with the Minister of Finance to increase Kāinga Ora's private debt limit by \$650 million to \$3.7 billion to enable the delivery of transitional places (between CHPs and Kāinga Ora) this financial year and begin work on the FY21 and FY22 programme;
- k. **Note** that in addition to taking a broader view on how Kāinga Ora should be enabled to deliver with partners on wider Housing and Urban Development system outcomes, the June 2020 report back will provide you and the Minister of Finance with the opportunity to make further decisions around:
 - i. Reducing funding and financing requirements through alternative phasing options, options to adjust the mix of locations and modes of delivery, and
 - ii. Options around providing new or increased subsidies for certain projects/loss making activities;
- l. **Note** agreement to a higher debt protocol would not constitute approval for investment decisions which will continue to be made through detailed Programme Business Case disciplines which provide for a consultation process with the Kāinga Ora Board and, you, where these are over agreed thresholds;
- m. **Note** pursuant to section 160 (1b) of the Crown Entities Act 2004 the approval for an increase in the debt protocol can be given jointly by the Minister of Finance and the Minister responsible for the portfolio.
- n. **Note** that while you are not required to consult Cabinet on a decision to increase the debt protocol, you may nevertheless choose to do so;
- o. **Agree** to discuss with the Minister of Finance an increase in the private debt facility for Kāinga Ora to \$7.1 billion to enable the organisation to deliver on short-term commitments and maintain momentum;
- p. **Note** that Treasury have been consulted and will be providing their own advice to the Minister of Finance;
- q. **Note** that Kāinga Ora will provide the Ministry of Housing and Urban Development with quarterly reports on current levels of debt, an updated debt forecast and progress against key programmes. The details of these reports will be agreed between Kāinga Ora and HUD by the end of 2019;
- r. **Forward** a copy of this briefing to the Minister of Finance; and

- s. **Note** that, subject to the outcome of discussions with the Minister of Finance, that officials will prepare an approval document to give effect to the recommended increase in the debt protocol, and a Cabinet paper should you wish to consult Cabinet on your decision.



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Place-based Policy and Programmes,
Ministry of Housing and Urban Development



Gareth Stiven
Deputy Chief Executive
Strategy and Investment
Kāinga Ora – Homes and Communities

Noted/Approved/Not Approved/Other

Hon Dr Megan Woods
Minister of Housing

Date

Purpose

- 21 This briefing is the first of two agreed reports back [BRF 19/20090412]. It provides you with advice on short term options to maintain momentum on Kāinga Ora's existing work programme in order to deliver Government priorities while minimising whole of government costs and staying within prudent borrowing limits. The briefing sets out financing options, including increasing the existing debt ceiling. It also provides advice on new initiatives agreed to by Ministers where decisions on financing are needed to be made now or imminently and decisions for Budget 2020.
- 22 The second report back will provide advice to enable Ministers to make decisions by June 2020 on the medium-longer term funding and financing arrangements for Kāinga Ora. This will include advice on how to fund and finance large scale projects and new activities.

Current Funding and Financing Model

- 23 Kāinga Ora has inherited Housing New Zealand's existing funding and financing model, which primarily consists of:
- core obligations around stewardship of existing stock, and provision of tenancy management services being more than met through the rental cash-flows of the business over time which drive free cash flows of circa \$380 million per annum;
 - debt being utilised to support capital investment (renewal and growth), which is serviced over time by surplus cash and rents, asset sales and/or appropriations;
 - growth in the state housing supply being funded from rental income (including the Income Related Rents Subsidy) from additional homes, asset sales and assumed government funded operating supplements (equivalent on average to 50 per cent of the market rent outside of Auckland).
- 24 In the year to June 2019 the main sources of annual funding for Housing New Zealand were the Income Related Rent Subsidy (IRRS) (\$880 million, 61% of revenue), rents received from tenants (\$471 million, 29% of revenue) and other Crown appropriations (\$102 million, 7% of revenue).
- 25 Kāinga Ora and its issuing subsidiary (Housing New Zealand Limited) is currently only one of two social housing providers to globally hold an Aaa credit rating from Moody's Investor Services. It is the only other Crown-owned entity to achieve this rating.

Origins of the Current Debt Limit of \$3.05 billion

- 26 In June 2018 Ministers approved a debt limit of \$3.05 billion to support the delivery of Housing New Zealand's (now Kāinga Ora) approved budgets in May 2018 as set out by its Board in its Long-term Investment Plan (LTIP). Specifically these budgets were intended to deliver over a four year period to June 2022;
- 4,480 more IRRS homes.
 - 6,901 new built homes.
 - 2,660 affordable and market homes enabled through land development.
 - Baseline planned maintenance programmes to support the delivery of well maintained, safe, warm and dry homes.
 - Commencement of the retrofit programme to a moderate standard including thermal uplift.

- Provision of tenancy support services to tenants.
- 27 The organisations LTIP is based on a range of key assumptions around costs, inflation, interest rates, sales revenues, scope (managing and maintaining existing assets to required standards, service levels etc.), and assuming market rent for all stock (underpinned by the IRRS), all of which have a material bearing on the sustainability of the LTIP.
- 28 As identified in the briefing note 'Long Term Investment Plan assumptions reviewed' dated 25 March 2019 [AH 19 016] and the briefing note 'Proposal to Increase the Debt Protocol' in April 2019 [BN/19/009] since the completion of the 2018 LTIP Housing New Zealand (and subsequently Kāinga Ora) has tested a number of these assumptions, and are beginning to confront decisions relating to trade offs around quality, cost, volume, and desire to support wider housing outcomes. This is driven by:
- timing changes, including additional buy-ins, costs associated with the Tamaki regeneration programme and delayed land sales, and
 - scope and quality changes in homes, including implementation of the Healthy Homes Standard, heating policy changes and proposed changes to the scope of our renewal and upgrade programme and additional refugee homes
 - cost increases, as a result of delayed contractual savings and land remediation,
 - revenue reductions as a result of the softening housing market
 - offset in part by a reduction in short term investments
- 29 Since April 2019, further changes include PERM, provisions for land development activity and the inclusion of contingencies to cover potential cost or timing changes.
- 30 In addition, it should be noted that the \$3.05 billion did not include provisions for Kāinga Ora to contract activity ahead of delivery (forward commitments).
- 31 These changes in key assumptions have had significant implications in terms of Kāinga Ora's approved debt limits and the timing of necessary changes to the debt protocol, and the organisations' long-term trajectory for growth and/or operating supplement settings.

Existing plans and commitments over the next four years

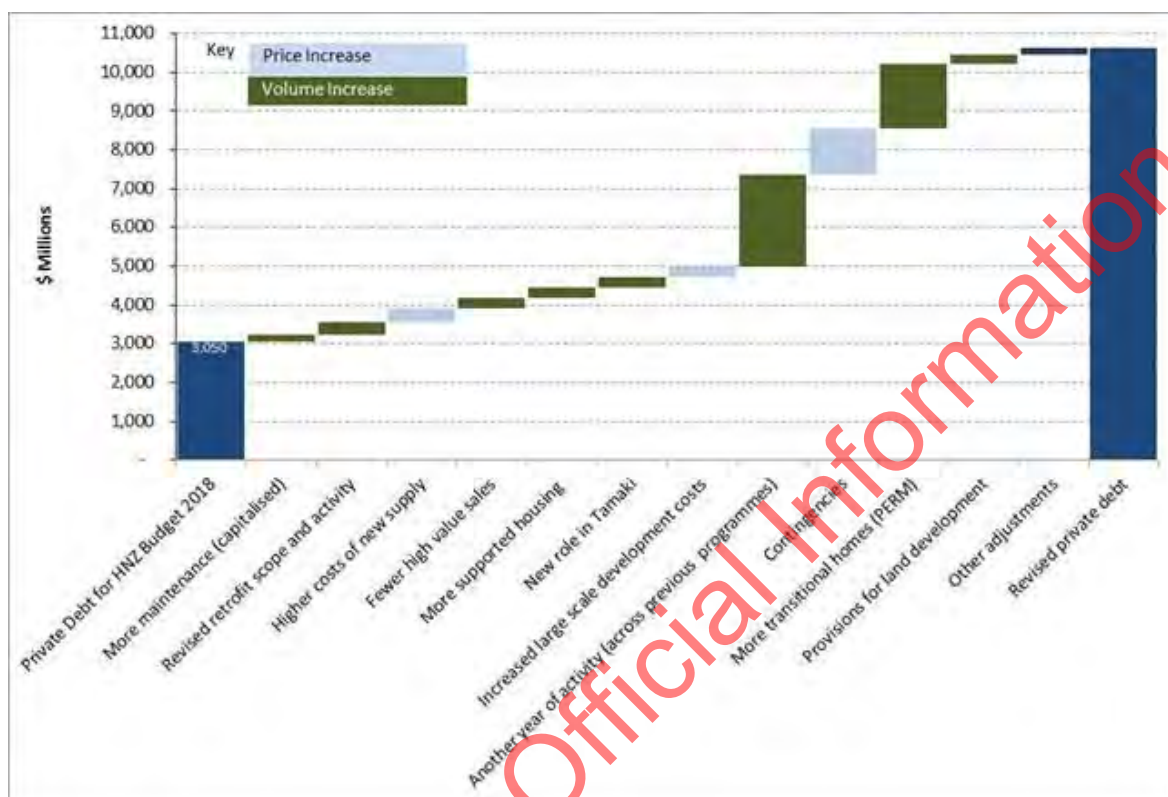
- 32 Kāinga Ora has also inherited existing plans with varying levels of commitment over the next four years. These include:
- legislative commitments
 - contracted projects
 - projects with approved business cases but which are not yet contracted
 - projects or programmes that have been announced by Ministers but are still pending completion of business cases
 - Medium- or longer-term plans with no specific formal commitment.
- 33 The table below sets out Kāinga Ora's existing plans and the level of commitment over the next four years and what will be delivered as a result of these. Further detail is provided in appendix three.

Programme	What the programme delivers over 4 years	Degree of commitment
Maintenance (capitalised)	65,300 well maintained homes Major components replaced (e.g. roofs). Compliance with Healthy Homes legislation (intervention in ~60,000 homes over four years). Complexes remediated (containing over 500 flats) over 4 years.	Legislative, contracted and/or essential commitments
Retrofits	Stage 1 of the retrofit programme (2019-2022) will bring 1,500-2,200 homes to a modern standard and made fit for another 50 years. Safe, warm, dry and functional homes matched to tenant needs.	Contracted commitment for first year HNZ Board agreed plan for 3-year trial.
	Commencement of stage 2 in FY23.	No commitment to stage 2.
Public Housing New Supply	4,480 additional IRRS homes in the 4 years to June 2022 as per Kāinga Ora's commitment to the Public Housing Plan. More families have access to safe, warm, dry and functional homes matched to their needs. Replacement of around 1,500 homes to access land to support this growth. Over 7,000 builds in the 4 years to June 2023, mostly through redeveloping Kāinga Ora land.	4,480 target Ministerial Announced ~40% of spend under contract or complete.
	Another 1,200 public houses in FY23 and replacement of homes to support this growth.	Ministers will make decisions as part of Budget 2020
Supported housing	Stage 1 transitional homes allowed for in HNZ May budget.	Ministerial Announced
	360 more homes to support increases in New Zealand refugee intake	Ministerial Announced
	115 homes for the Department of Corrections to assist reintegration of prisoners into communities	HNZ Board agreed
	Provision of more community group houses	Not announced or agreed.
Tamaki	Kāinga Ora role in financing the Tamaki Regeneration.	Ministerial Announced
Large scale development	Delivery of our Northcote, Mangere, Mt Roskill and Oranga urban development programmes delivering improved master planned communities, developed sites for new state housing and super-lots for sale for market/affordable homes	The HNZ Board reviewed the programmes in Sept 2019 and only agreed stages required to maintain momentum and meet commitments already made for delivery over the next 12-18 months.
Transitional homes to help permanently end reliance on motels	Delivery of around 700 transitional homes this year to help permanently end reliance on motels (PERM).	Ministerial Approved
	Provision for years two and three of PERM	Not approved.
Provisions for land development	Acquisition of new sites to support urban development	Not approved.
Contingencies	Contingencies to provide coverage for further price escalation, unanticipated ground conditions, infrastructure increases in essential works requirements and erosion of sales revenues	Not approved.

34 Refer to paragraph 50 for a detailed breakdown of what is expected to be delivered by year over the next four years.

35 Most of these programmes have identified funding streams and further funding is expected to be confirmed through Budget 2020. The draft new initiative *Homelessness Package: Public Housing Supply* seeks funding for up to 12,000 new IRRS places to be delivered by June 2024 by CHPs and Kāinga Ora. This would provide funding for the 2023 housing growth places and part fund years two and three of the PERM programme where those places are delivered as public housing. In addition to these Budget decisions Kāinga Ora will also need to make investment decisions in new land. Funding implications for these will need to be identified through subsequent business cases on an as required basis.

- 36 However as can be seen in the below figure these programmes will result in significant additional financing requirements for Kāinga Ora from what was anticipated in 2018. The biggest drivers of which are scope and volume increases associated with an additional year of growth and more transitional homes (PERM).



- 37 To deliver the benefits and programme of work agreed with the Government current modelling indicates that the organisation will need approximately \$10.7 billion comprised of :

- \$8.7 billion in debt to meet revised budget intentions, including new approved initiatives, cost increases and scope changes, and
- \$2 billion to additionally meet planned activity which consists of:
 - \$1.7 billion under the PERM initiative (of which \$650m has already been approved)
 - \$0.25 billion to provide provisions for new land development initiatives.

- 38 It should be noted that:

- The above analysis includes an assumption that Kiwibuild is a fully funded Crown programme [HUD briefing BRF 19/20090411 refers].
- Any additional new initiatives over the next 12 months will need to be agreed on a case-by-case basis with financing arrangements being revisited if significant new early investment is required.
- The following is currently excluded from this financing request:
 - Porirua (pending Board approval of a business case in the new year). Note a tagged contingency for Porirua East is being sought through Budget 2020 for supporting infrastructure to enable the first neighbourhood redevelopment.
 - New land development activity beyond first two-year provisions.

Implications for the debt protocol

- 39 Kāinga Ora currently has a borrowing protocol limit of \$3.05 billion based on the debt required to meet its obligations for the four years ending June 2022. This included delivery of the 4,480 new public housing places announced in Budget 2018; and advancing the Auckland Housing Programme projects at Mangere, Mt Roskill, Oranga and Northcote.
- 40 It was assumed as part of the 2018 Housing New Zealand Long-term Investment Programme (LTIP) that over time this debt level would increase to fund and finance the plan, driven by assumed additional growth and renewal costs. It was anticipated in the LTIP that debt levels would continue to grow, peaking at just over \$10 billion.
- 41 Kāinga Ora signalled in April this year that the current debt protocol limit of \$3.05 billion agreed with Ministers was not enough to allow it to deliver its four-year budget intentions. Kāinga Ora now expects to reach its private debt cap by mid-2020 meaning it will no longer be able to sign new contracts from around February 2020 (essentially a contracted breach i.e. Kāinga Ora will need to contract delivery in advance to paying for delivery).
- 42 This is due to a range of underlying factors (as indicated in the section prior) including new activities, scope changes, unforeseen events, changing market conditions, delayed realisation of scale and innovation efficiencies, and changes to dwellings mixes, delivery timeframes and yields. This has resulted in costs being higher than budgeted (notably for land remediation, construction and infrastructure) and revenues lower than anticipated (including due to an unanticipated drop in land values and increased levels of affordable housing).
- 43 Kāinga Ora is currently operating within its current debt protocol limit of \$3.05 billion for private debt.

Proposed approach

- 44 We are proposing a two-pronged approach to address the current funding and financing issues:
- a) Short-term: Addressed in this paper and covering options for reducing spend in the short-term and immediate financing requirements
 - b) Medium-term: A full review of Kāinga Ora's funding and financing arrangements to be undertaken in time for the June report back which will give you the opportunity to make decisions around:
 - Reducing funding and financing requirements through alternative phasing options, options to adjust the mix of locations and modes of delivery, and
 - Options around providing new or increased subsidies for certain projects/loss making activities.
- 45 This approach is discussed in more detail in the below sections.

Short-term approach

Short-term: Options for reducing spend

- 46 Initial estimates suggest that there are few gains to be had in deferring elements of the activity forecasted in the short-term to keep debt below current limits, primarily due to the relative low cost of debt compared with construction cost inflation but also as the majority of the first two years, due to the nature Kāinga Ora's business, is largely committed or essential spend.

47 Kāinga Ora has not considered options to reduce core maintenance and asset renewal obligations as this is a fundamental responsibility of a prudent asset owner. As such the major lever to reduce spend would be to reduce the growth of public housing which would see Kāinga Ora not meet its commitment to the delivery of the balance of the 4480 additional IRRS places.

48 The table below references the status of proposed spend for the two years ending June 2021.

Category and Programmes	Deliverables	Financing Required (\$ million)
Opening Private Debt		\$1,550.0m
Operating cash flows (after interest and tax)		-\$656.1m
Sales Revenues		-\$94.2m
Firm commitments within current funding and financing (core business as usual and legislative and contracted projects)		
Maintenance Capitalised	Homes well maintained, healthy homes compliance and block remediation.	\$341.2m
Retrofits	First year committed spend on 300-400 homes and planned lifecycle spend next year on 500-800 homes	\$207.9m
Supported housing	Stage 1 transitional housing, refugee and corrections housing	\$139.5m
Tamaki Regeneration		\$229.5m
Transitional homes to help permanently end reliance on motels	Around 700 transitional homes by June 2020.	\$634.5m
Corporate capital	Capital spend to support corporate services	\$46.6m
Sub-Total		\$1,599.2m
Firm commitments announced by Ministers that were adequately funded and financed, but costs and/or anticipated revenue have shifted		
New Supply programme to deliver IRRS homes	3,616 new built homes resulting in net 2,240 homes towards public housing plan.	\$2,252.4m
Large scale redevelopment programme	Progression of Northcote, Mt Roskill, Mangere and Oranga urban development	\$102.1m
Contingencies	Coverage for further price escalation, unanticipated ground conditions, infrastructure increases in essential works requirements and erosion of sales revenues	\$731.2m
Sub-Total		\$3,085.7m
Plans endorsed by the HNZ Board, including those without funding		
New Community Group homes	New homes to support community group providers	\$44.0m
Transitional homes to help permanently end reliance on motels (second year spend)	1,000 transitional homes next year	\$616.0m
Provision for land development	New land for urban development	\$250.0m
Provision to meet forward contract commitments	Debt protocol to cover forward contract commitments	\$587.6m
Retrofits	Thermal, functional and accessibility improvements planned for next year on 500-800 homes	\$84.0m
Sub-Total		\$1,581.6m
Total		\$7,066.2m

Short-term: Immediate financing requirements

- 49 As indicated in the prior sections, Kāinga Ora will require financing of \$10.6 billion to maintain momentum on its existing commitments and deliver proposed new activity over the four-year period. As is detailed in Appendix 1 this is comprised of:

Option	Allows Kāinga Ora to:	Risks	Additional finance total required (\$b)	Increase relative to current protocol(\$b)
0	Current debt protocol	\$3.05 billion to deliver the first two years of budget intentions (but did not include provisions for activity to be contracted ahead of delivery and \$650 million to enable the delivery of transitional places (between CHPs and Kāinga Ora) this financial year and begin work on the FY21 and FY22 programme	Would undermine ability to meet existing growth commitments	\$3.7
1	Forecast activity until June 2020	Have debt limit to enable budget intentions to June 2020, meet first year of PERM, sign some contracts for 2021 onwards and have provisions for new land development activities.	Would require the protocol to move by 1 July next year and/or other financing arrangements agreed. Any delays in decision making would materially affect Kāinga Ora's ability to operate from 1 July 2020.	\$4.554
2	Forecast activity until June 2021 (Recommended)	Have debt limit to enable budget intentions to June 2021, meet first two years of PERM, sign some contracts for 2022 onwards and have provisions for new land development activities.	Will require a reset of the debt protocol limit following June report back.	\$7.066
3	Forecast activity until June 2023	Have debt limit to enable the full four-year Kāinga Ora investment profile.	Yet to work through key investment and funding decisions. Preferred option is to address this through June report back.	\$10.614

- 50 The following table sets out the key Kāinga Ora deliverables under each option;

		FY19+20 Option 1	FY21 Option 2	FY22	FY23 Option 3
Private debt required for Budget Intentions	\$b	\$3.228	\$4.978	\$6.842	\$8.701
Key cumulative deliverables we get for that debt					
Contribution to 4,480 more IRRS homes	#	2,342	3,462	4,480	
More homes for refugees	#	75	150	255	360
Gross homes built by Kāinga Ora	#	3,239	5,064	6,914	8,699
Home retrofitted	#	300-400	800-1,200	1,500-2,200	3,000-3,700
Market/affordable homes enabled	#	1,073	1,774	3,069	3,153
Compliance with new Healthy Homes legislation					Yes
Private debt required for Other Activities	\$b	\$0.760	\$1.500	\$1.923	\$1.913
Key cumulative deliverables we get for that debt					
New transitional homes through PERM	#	~700	~1,700	~2,900	
New land for development	#	tbc	tbc	tbc	tbc
Provisions for forward contractual commitments	\$b	\$0.566	\$0.588	\$0.490	\$0.000
Private debt required in total	\$b	\$4.554	\$7.066	\$9.255	\$10.614

- 51 It is recommended that approval be given for Kāinga Ora's to borrow up to \$7.1 billion in line with the above table above noting that the organisation will come back to you in June with a more comprehensive, longer-term view of funding and financing requirements for the organisation.

- 52 Without additional financing Kāinga Ora will need to put current programmes on hold as early as February 2020. It has taken Kāinga Ora years to achieve the scale and pace it is currently delivering, regaining lost momentum would take time and likely have financial and reputational issues for the organisation.

Short-term: Financing Options

- 53 There are three alternative avenues for financing the capital spending requirements of Kāinga Ora:

- Option (a) Private borrowing by Kāinga Ora which would not impact core crown and would not count against Budget 20 capital allowances; OR
- Option (b) Crown lending to Kāinga Ora which would have an initial impact on gross debt and net debt but will be neutral over time and would not count against Budget 20 capital allowances, if lending is repaid within 10 years; OR
- Option (c) An equity injection for Kāinga Ora which would impact net debt, but the impact is managed through budget allowances.

- 54 Choosing between these options or a mix depends the preferences that Ministers have for:

- minimising whole of Government costs and providing the Minister of Finance with optimum oversight of whole of Government debt; (You would favour option (b))
- providing Kāinga Ora with the business and investment flexibility that it seeks (You would favour option (a)); and
- confidence that the increased debt incurred under Option (a) will remain within prudent limits (In the absence of such confidence you would curtail both options (a) and (b) and adopt option (c)).

- 55 Option (c) - capital injection would be an important option to consider if the proposed debt would otherwise exceed prudent levels. However, Kāinga Ora is confident that this is not yet an issue. Options for capital injection and other Crown funding options will be provided in the June 2020 report back.

Recommendation

- 56 It is recommended that these funds are borrowed externally, particularly in the short term, given the need for financing (DMO approval would mean this would be delayed until June and alternative financing would be required to get Kāinga Ora through to this point) requiring an approval from you to increase in the current debt protocol limit.

- 57 While Kāinga Ora would not get the benefit of lower DMO interest rates through this option, the greater flexibility and certainty allowed for with private borrowing would allow it to continue to enter into long-term supplier arrangements. Over the last year the long-term supplier arrangements that Kāinga Ora have entered have resulted in an approximate 15% reduction in build costs.

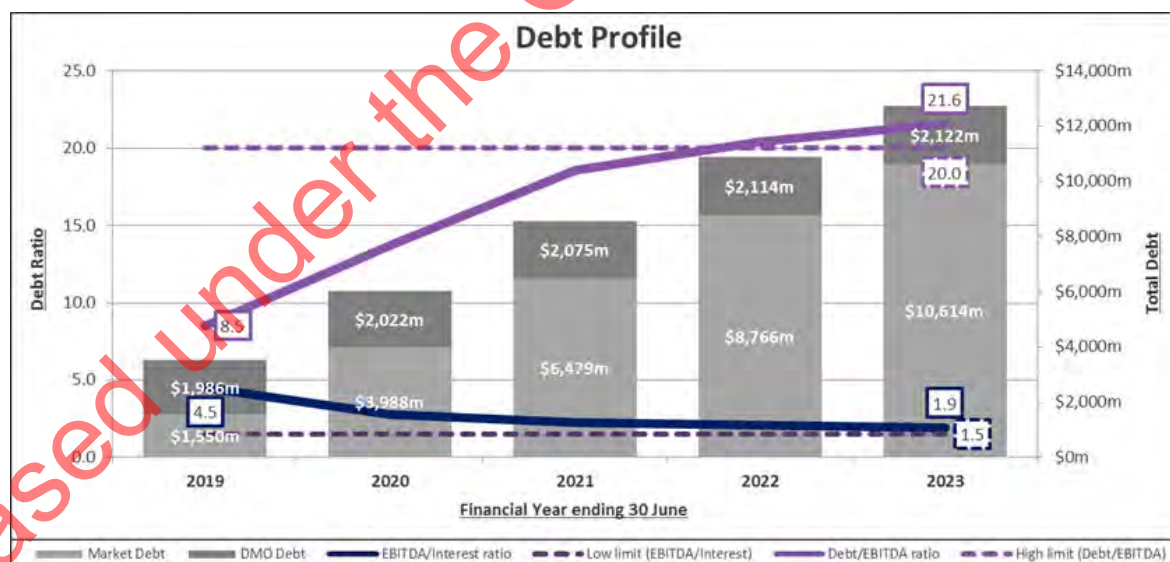
- 58 This position however can be reassessed through the June report back.

Sustainability of increased debt

- 59 Approval of an increased debt limit would enable Kāinga Ora to transact decisions up to an agreed amount. Agreement of a limit would not provide approval for investment decisions. Investment decisions are and will continue to be made

through detailed Programme Business Case disciplines which provide for a consultation process with the Kāinga Ora Board and yourself where these are over agreed thresholds.

- 60 It is also important to note that this debt would be utilised in line with Kāinga Ora's key Long-term Investment Plan principle to only invest in assets (for renewal and growth) and that the Crown largely determines the drawdown of this debt through its funding decisions i.e. if IRRS were limited Kāinga Ora would not grow its portfolio.
- 61 The organisation's forecast debt profile is shown in the following chart. A key indicator is the "Debt/EBITDA ratio. This compares a company's total obligations, including debt and other liabilities, to the actual cash the company brings in. It reveals to lenders and shareholders how capable a company is of paying its debt and other liabilities. As can be seen in this figure, the approval of a \$7.1 billion debt limit to enable budget intentions to June 2021 would allow the organisations prudence measures to stay within acceptable ranges over the next 18 months.
- 62 The increased levels of debt resulting from Kāinga Ora's full four-year investment profile would result in \$10.6 billion private debt, which would take current prudence metrics to capacity, though even at \$10.6 billion Kāinga Ora is still able to pay interest 1.9 times. This shows there is sufficient income to meet interest servicing obligations. However, this highlights the importance of income certainty to Kāinga Ora so that it can service its debt and that there is activity that Kāinga Ora is doing now that does not currently have income attached to it. For example supporting housing affordability, community and urban regeneration activity.
- 63 Levers to address this such as additional revenue streams, making adjustments to programme expenditure and equity injections will be discussed in Budget 2020 discussions and the June report back to Ministers.



- 64 For completeness it should be noted that this figure includes current Kāinga Ora DMO debt totalling \$2.122 billion. It should be noted that the assessment of Kāinga Ora's financial sustainability using debt profile metrics (e.g. Debt/EBITDA ratio) includes this debt, however this is treated as an interest only loan in the Kāinga Ora LTIP, with no principle repayment until all private finance is repaid (forecasted circa 2070).
- 65 Kāinga Ora's baseline Long-term Investment Plan projects that to deliver its current forecasted activity private debt will need to peak at approximately \$17 billion, with a

debt to revenue ratio of approximately 640% and debt to asset ratio of 34%. This is because the debt is being spent on revenue generating assets and shows that while Kāinga Ora's stand-alone credit profile (i.e. without any assumption regarding Crown support) would temporarily weaken, the debt is sustainable in the long term. This confirms that while the organisations' current investment intentions are high, it is still anticipated Kāinga Ora would be able to be sustainable from a stand-alone perspective.

- 66 For context it should be noted that in the 1980's Housing New Zealand Corporation's debt to revenue ratio peaked at 1,300% and debt to assets ratio peaked at 95%.

Medium-term approach – June report back

- 67 It is proposed the June report back will build on the decisions sought in this paper around the short-term funding and financing requirements for Kāinga Ora's current project pipeline by taking a broader view on how Kāinga Ora can best be enabled to deliver with partners on the wider outcomes sought for the Housing and Urban Development system. This advice which will be developed between HUD and Kāinga Ora will:

- Confirm the outcomes sought and how the known pipeline of projects will be prioritised to deliver them,
- Separately and transparently set medium to long term objectives and funding levels for each of the main areas of activity for Kāinga Ora,
- Agree a prudent and sustainable debt profile through time and other associated funding requirements, and
- Integrate the funding and financing model for Kāinga Ora with other workstreams underway such as the Public Housing Funding Review and Procurement Plan.

- 68 To support these decisions, it should be noted that Kāinga Ora has several pieces of work underway including:

- Large scale programmes. The Housing New Zealand Board reviewed the large-scale programmes in September 2019 and only agreed stages required to maintain momentum and meet commitments already made for delivery over the next 12-18 months. The remaining elements of the large-scale programmes were put on hold pending a broader review which will consider:
 - From a bottom up perspective standards and services levels relating to civil works and the approach to managing infrastructure costs
 - From a top down perspective whether the large-scale approach is the best mechanism for achieving the outcomes the crown is seeking
 - A broader review comparing greenfield vs brownfield development approaches
- Development of the Porirua business case

Risks and mitigations

Risk	Likelihood	Impact	Mitigation
Debt protocol limit is raised incorporating investment activities that may be deprioritised through the June report back.	Low All seen as essential spend to meet crown priorities	Moderate Investment can be deprioritised	<ul style="list-style-type: none"> • Agreement of the debt protocol limit is not the mechanism to approve investment spend or priority. • All investment to draw down on debt will be underpinned by a relevant business investment case following agreed delegated approvals.
Protocol limit is insufficient to cover current and new activities.	Moderate Likely driven from new activity	High We would need to review the limit sooner than expected	<ul style="list-style-type: none"> • There is an opportunity to raise limits again mid way through next year through the June report back. • Significant new investment proposals could be developed with their own recommendations on debt limits. • Contingencies are included in the protocol limit. • We recommend having the limit set for the investment plan to the end June 2021.
The funding required to implement the investment plan is not put in place.	Low Mechanisms in place	High We could not commence activity	<ul style="list-style-type: none"> • There is a clear strategy around Budget 2020 funding decisions. • June report back will address medium term investment priorities and funding.

Reporting and Monitoring

- 69 In order to provide you with confidence around the effectiveness of Kāinga Ora's spend the organisation intends to provide you with quarterly reports on current levels of debt, an updated debt forecast and progress against key programmes. The details of these reports will be agreed between Kāinga Ora and HUD by the end of 2019.

Next steps

- 70 Pursuant to section 160 (1b) of the Crown Entities Act 2004 the approval of an increase in the debt protocol must be jointly given by the Minister of Finance and the Minister Responsible for the portfolio.
- 71 The Cabinet Manual advises that matters should be submitted to Cabinet if they involve proposals that affect the government's financial position or constitute important financial commitments. This is a significant decision that warrants consideration by Cabinet. You may wish to discuss this with the Minister of Finance.
- 72 We recommend that you forward a copy of this report to the Minister for Finance.
- 73 We would welcome discussion with you on any of the points raised in this paper.



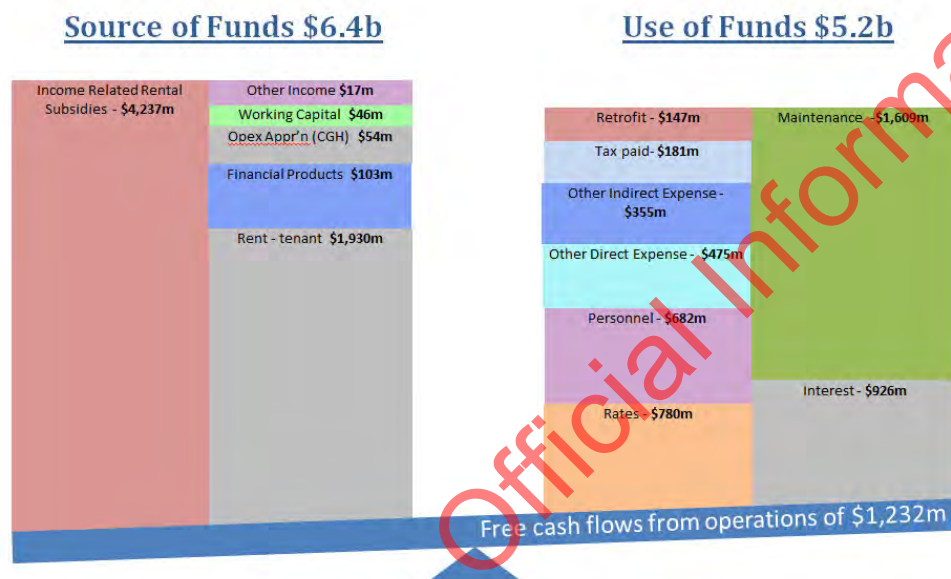
Appendix One – Anticipated benefits from Kāinga Ora Investment Activity

	Upgrade and Renewal	Growth	Urban renewal
Tenants	<ul style="list-style-type: none"> • Social housing continues to be available • Improved physical and mental health from retrofitting insulation and heating • Reduced time in hospital and being sick • Reduced risk of respiratory, cardiovascular and infectious illnesses • Reduced operating costs • More days in school for kids • Reduced time off work • Improved social inclusion and economic outcome • More stable housing leads to higher functioning children and better social integration • Safer homes leading to fewer injuries – less slips, trips & falls. • Better matched homes • Reduction in prison time in preference to home detention • Reduced mortality particularly for elderly people. 	<ul style="list-style-type: none"> • Improved health and wellbeing • Improved social inclusion and economic outcome • People in the right home for their family • Helps refugees better settle in NZ • Stable housing solution for homeless • Help transition NZer's into stable housing • Improved well being for people with disabilities 	<ul style="list-style-type: none"> • More cohesive, supportive communities • Safer communities • Better physical environment • Removal of stigma • Greater lifestyle choices • Creation of employment opportunities • Lower costs to individuals
Govt	<ul style="list-style-type: none"> • Improved social inclusion and economic outcome • Safer homes leading to fewer injuries • No need for Crown Investment in Kāinga Ora • Reduced Greenhouse emissions • Reduced injuries and ACC payments 	<ul style="list-style-type: none"> • Reduced Public Housing Register • Improved health and wellbeing • Improved social inclusion and economic outcome • People in the right home for their family • Helps refugees better settle in NZ • Stable housing solution for homeless • Help transition NZer's into stable housing • Improved well being for people with disabilities 	<ul style="list-style-type: none"> • Increased home ownership options • Pride and stability of ownership strengthens communities • More people access the 'capital' benefits of homes ownership • Greater lifestyle choices • Safer communities • Creation of employment opportunities • Lower costs to the Crown
Kāinga Ora	<ul style="list-style-type: none"> • Reduced maintenance costs • Increased market rent • Increased Capital Value of homes • Improved customer satisfaction • Debt levels can be managed • Efficient build processes 	<ul style="list-style-type: none"> • Reduced Public Housing register • More social homes • Social housing continues to meet long term needs 	<ul style="list-style-type: none"> • Improved value of housing assets • More efficient use of land • More homes in urban areas

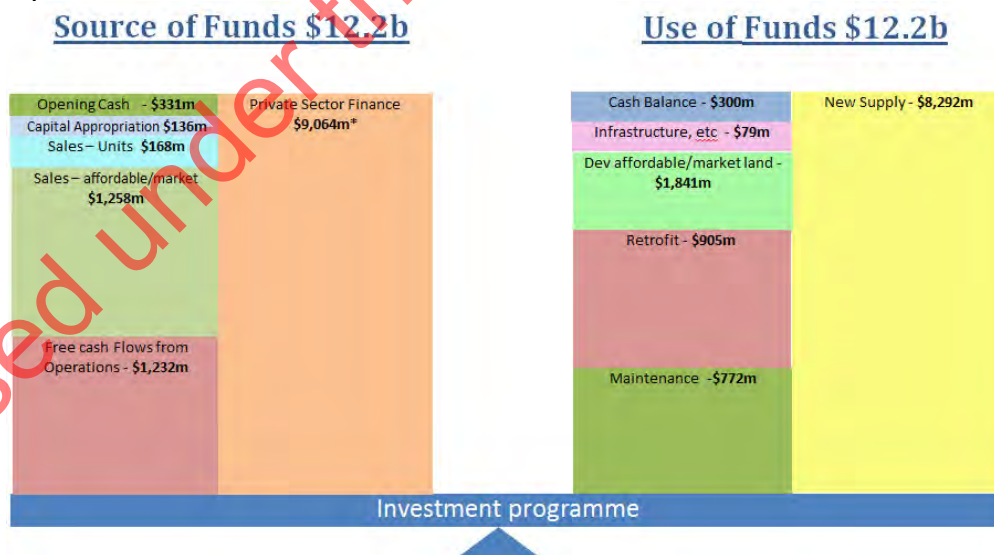
Appendix Two– Kāinga Ora Sources and Uses of Funds 2019-2023

The following figure summarises Kāinga Ora's key sources and uses of funds over the next four years².

Operating position



Capital position



² Projected private sector debt at June 2023 (\$10,614m) comprises opening private debt at June 2019 (\$1,550m) plus incremental private debt financed over the 4 years to June 2023 (\$9,064m)

Appendix Three – Kāinga Ora funding and financing requirements 2019-2023

Programme	Description	Programme Status	Driver for budget increase	Options or alternatives	Financing View						Effect of reduced activity	Primary Funding Source and Status
					Existing Budget (B2018)	+Budget Increase	+Additional Year	= 4-year Budget (B2019)	Committed Spend	Non – Committed Spend		
Managing and Maintaining the Public Housing Portfolio												
Complex Remediation	Remediation of older Kāinga Ora housing blocks. Often including seismic upgrades.	Under construction, procurement and planning.	Cost Increases	None recommended.	\$21m	+\$13m (+60%)	+\$7m	\$41m For 508 units upgraded	\$41m Essential spend	Nil	People living in older complexes for longer – reduced wellbeing. Would result in extra opex spend and lost income. Reputational and RTA risk.	Market rents ³
Healthy Homes	Legislated implementation of the Healthy Homes Standard.	Commenced for completion 2023.	Quality and scope changes	Legislated - no options except could potentially allow slower path for Kāinga Ora.	\$0m	+\$170m	+\$73m	\$243m Portfolio spend	\$243m Legislative spend	Nil	n/a	Market rents
Heating Policy	Ensuring adequate heating of homes, rolled out along side Healthy Homes.	Option adopted by board to enhance standards.	Quality and scope changes	None recommended. Could rescind or slow this policy to align with renewal and upgrade programme.	\$0m	+\$49m	+\$19m	\$68m Portfolio spend	\$68m Essential spend	Nil	Tenants unable to heat their homes to the Board agreed standards.	Market rents Small uplift in rents resulting from higher standards
Retrofits	Upgrade of older state homes to make them fit for purpose for the next 50 years. Includes addressing	Board approved business case for stage 1. Though expenditure permissions given	Quality and scope changes	Cheaper options available by dropping; • accessibility (\$122m)	\$198m	+\$339m (+170%) But costs	\$368m	\$905m For up to 3,700 homes	\$96m First year	\$231m enhanced accessible/functional scope	Fundamental shortfalls in housing performance not addressed.	Market rents Small uplift in rents resulting from higher

³ Note these market rents include the Income Related Rent Subsidy (i.e. around 2/3rds of Kāinga Ora's rental income is paid for by the Crown)

Programme	Description	Programme Status	Driver for budget increase	Options or alternatives	Financing View						Effect of reduced activity	Primary Funding Source and Status
					Existing Budget (B2018)	+Budget Increase	+Additional Year	= 4-year Budget (B2019)	Committed Spend	Non – Committed Spend		
	deferred maintenance, essential lifecycle works (e.g. reroof), accessibility, functional and thermal upgrades.	for FY20 only with works currently being rolled-out.	\$8.6m works carried forward.	<ul style="list-style-type: none"> functionality (\$109m) thermal (\$116m) 		largely offset through future maintenance savings		retrofitted			Tenants wellbeing impacted.	standards
										\$116m thermal uplift	Thermal underperformance of homes not addressed. Wellbeing of tenants impacted.	Market rents Small uplift in rents resulting from higher standards.
										\$462m essential, lifecycle works and deferred maintenance	Works deferred but problem does not go away. Would result in extra opex spend until works completed or homes sold.	Market rents Ongoing whole of life savings in maintenance and other planned maintenance
Ongoing maintenance	Capitalised spend on repair and maintenance of Kāinga Ora homes. Includes responsive repairs, upgrades under the void programme, meth reinstatement, roof replacement and other planned works.	Required to ensure Kāinga Ora service levels and legislative requirements (e.g. RTA).	Savings Retrofits competing more ongoing maintenance. Savings ongoing.	None recommended.	\$258m	-\$42m (-16%)	+\$80m	\$296m Portfolio spend	\$296m Essential spend	Nil	Works deferred but problem does not go away. Would result in extra opex spend until works completed or homes sold. Reputational and RTA risk.	Market rents
Other planned maintenance	Range of initiatives aimed at supporting the service levels of the Kāinga Ora portfolio.	Ongoing investment.	Savings Retrofits competing more other maintenance	None recommended.	\$71m	-\$22m (-30%)	\$16m	\$65m Portfolio spend	\$65m Essential spend	Nil	n/a	Market rents

Programme	Description	Programme Status	Driver for budget increase	Options or alternatives	Financing View						Effect of reduced activity	Primary Funding Source and Status
					Existing Budget (B2018)	+Budget Increase	+Additional Year	= 4-year Budget (B2019)	Committed Spend	Non – Committed Spend		
PBMC Fees	Externalised management of the Kāinga Ora maintenance and upgrade programme.	Current contract to June 2020. New contract currently out for tender.	Scaled Spend with more works completed	Essential management of programme works, but would scale up or down commensurate to amount of works completed.	\$33m	+\$12m (+36%)	+\$15m	\$60m	\$60m Margin based spend	Nil	No/limited possible reduction in works covered by this contract. Extra costs of internalising activities.	Market rents
Totals for Managing and Maintaining the Public Housing Portfolio					\$582m	\$518	+\$578m	\$1,678m	\$869m	\$809m		

Programme	Description	Programme Status	Driver for budget increase	Options or alternatives	Financing View						Effect of reduced activity	Primary Funding Source and Status
					Existing Budget (B2018)	+Budget Increase	+Additio nal Year	= 4 year Budget (B2019)	Committ ed Spend	Non – Committed Spend		
Growing the Public Housing Portfolio												
Replacement & new IRRS supply	Kāinga Ora new supply programme to replace and grow homes to meet Public Housing Plan Targets	As per Budget 2020 commitments. Build costs savings are beginning to come though in recent contracts, but significant volume already in play and prevailing rates.	Cost and mix increases Change in programme mix from builds to buy-ins.	None, accept slowing or reducing programme. No commitment to FY 23 at this stage. But, capacity contracts in place. Could defer decision in FY23 but need for this supply unlikely to abate.	\$2,844m	+\$350m (+12%)	+\$1,215m	\$4,410m For 3,408 homes replaced and 4,480 new IRRS homes in 4 years to June 2022. Another 1,200 growth for FY23.	\$867m already contracte d	\$2,209m Supply contributin g to Public Housing target.	Failure to meet Budget 2018 commitments and housing register not reduced.	Market rents + OS provisions provided through Budget 2018 Net Sales Revenues
									\$40m	\$1,174m FY23 supply.	Inability of Kāinga Ora to contract FY23 supply. With 12-24-month approval lead in time decisions on this will need to be made by Budget 2021. Limits ability to enter and roll-over capacity-based contracts, increasing delivery costs.	IRRS not yet funded
										Up to \$120m By deferring Kāinga Ora Kiwibuild	Replacements partly linked to Large Scale Redevelopment programme. Some ability to defer based on decisions for those programmes.	Market rents

Programme	Description	Programme Status	Driver for budget increase	Options or alternatives	Financing View						Effect of reduced activity	Primary Funding Source and Status
					Existing Budget (B2018)	+Budget Increase	+Additional Year	= 4 year Budget (B2019)	Committed Spend	Non – Committed Spend		
State house sales (incl McLennan)	Sale of Kāinga Ora state houses and vacant land.	Ongoing. Delays in the sale of high-value property, predominantly in Auckland central and the North Shore.	Timing	Could be accelerated. Limited rehousing opportunities have made this difficult.	-\$406m	+\$270m	-\$42m	-\$178m From 400 sales	-\$178m	Nil	n/a	n/a
Greys Ave	Building specialised block for high need tenants in Central Auckland.	Project approved by HNZ Board. In Planning.	Volume increase New initiative since Budget 2018	Defer Scale back on private homes and spaces.	\$0m	\$0m	+\$197m	\$197m For 76 market homes and 200 public housing units	\$14m	Up to \$183m	Very high social cost of not proceeding. Cost and reputation issues.	IRRS/operating costs not yet funded (now that it is in FY23 for delivery)
Refugees	Increased Volume	Planning under way. No approval to drawdown.	Volume increase New initiative since Budget 2018	Scale Kāinga Ora contribution	\$0m	+\$146m	+\$49m	\$195m For 360 homes	Minor	\$195m	Fewer public homes to meet increased refugee intake.	Funded in contingencies
Corrections	New Activity, rents funded by Corrections.	Programme under development.	Volume increase New initiative since Budget 2018	Defer	\$0m	+\$60m	\$0m	\$60m For 115 homes	Minor	Up to \$60m	Opportunity missed to partner with another crown agency to address ex-prisoner rehousing.	Corrections funded
Transitional Housing	Stage 1 New transitional housing funded externally. 500 transitional units/ buy-ins to meet current waiting list demands	Under review with decisions to be made under next budget.	Timing issue rental arrangements generally allow for debt to be paid down.	Defer	\$0m	+136m	+\$10m	\$146m	Minor	\$146m	Under review with decisions to be made under next budget.	IRRS/operating costs not funded
Community Group Housing	Additional activity	ET approved plan subject to LTIP and funding approval.	Volume increase New initiative	Scale-down or defer.	\$0m	+\$33m	+\$11m	\$44m	\$11m	\$33m	No new homes for community housing sector at	IRRS/operating costs not funded

Programme	Description	Programme Status	Driver for budget increase	Options or alternatives	Financing View						Effect of reduced activity	Primary Funding Source and Status
					Existing Budget (B2018)	+Budget Increase	+Additio nal Year	= 4 year Budget (B2019)	Committ ed Spend	Non – Committed Spend		
			since Budget 2018								time of high demand.	
Totals for Growing the Public Housing Portfolio					\$2,438m	\$994m	\$1,439m	\$4,872m	\$754m	\$4,118m		

Programme	Description	Programme Status	Driver for budget increase	Options or alternatives	Financing View						Effect of reduced activity	Primary Funding Source and Status
					Existing Budget (B2018)	+Budget Increase	+Additio nal Year	= 4-year Budget (B2019)	Committ ed Spend	Non – Committed Spend		
Urban Regeneration and Affordable Housing												
Tamaki Redevelopme nt	Kāinga Ora Financing of Tamaki Redevelopment. Assumed Cost neutral to Kāinga Ora in the long term.	Works commenced. \$745m costs, \$512m sales within period	Timing issue New initiative and role for Kāinga Ora.	Decisions not yet made, other financing options available.	\$0m	+\$279m	-\$45m	\$234m Refer TRC for outputs	Some	Up to \$234m	Need new financing structure for Tamaki Redevelopment Corporation activity.	Assumed Kāinga Ora recompensed for shortfalls (mechanism to be put in place)
Urban Development Group – Super lot delivery	Master planned development of Kāinga Ora land to provide super lots for state, market and affordable housing.	Gross budget \$688m largely offset by sales. Activity well underway.	Cost increases Permanent/ timing issue.	Little alternative – land that needs further remediation than expected and infrastructure being in worse condition or in some cases not there.	\$370m	+\$183m (+50%)	+\$135m	\$688m for 2,854 private/ affordabl e and 1,363 public enabled	\$307m Contract ed	\$380m Spend to enable land sales	Decisions could be made to reduce level of regeneration. May be difficult to extract volume and would reduce sales options.	Sales revenues Market rental increases. Funding for long-term potential shortfalls to be resolved.
Urban Development Group – Super lot sales		\$667m sales revenues from super lots sold.	Revenue reductions and timing issues Permanent/ timing issue.	Softening housing market and a change to the mix in market and affordable housing.	-\$551m	+89m (-16%)	-\$206m	-\$667m	-\$385m Sales enabled by Contract ed spend	-\$282m Sales enabled	n/a	
KiwiBuild by Kāinga Ora	Building KiwiBuild product on previous Kainga Ora land	\$408m gross builds. Build projects commenced.	Volume increase New initiative provisions only.	Pull back on activity.	\$0	\$304m	\$104m	\$408m	-	\$408m	Kāinga Ora need to demolish 200 existing homes to make way for the programme. Refer New IRRS section for offset.	Sales revenues of KiwiBuild homes
	Provisions only	\$408m gross sales revenues. No sales revenues to date		Pull back on activity.	\$0	-\$304m	-\$104m	-\$408m	-	-\$408m		
Totals for Urban Regeneration and Affordable Housing					\$-181m	+\$551m	-\$116m	\$254m	-\$78m	\$332m		

AH 22 077

15 July 2022

Hon Megan Woods, Minister of Housing
Cc Vui Mark Gosche, Board Chair



Financial Sustainability – Accessibility and HomeStar advice

Purpose

1. This advice responds to a request from you for further information on the delivery of accessibility and Homestar improvements to public housing to support budget discussions.

Background

2. In June 2022 we provided you with an update on the Kāinga Ora – Homes and Communities budget for 2022-26 and the implications of this on our longer term financial sustainability, in particular the impact of cost pressure and inflation and the implications of this on our funding settings, projected debt and our associated financing strategy (BN 22 015 refers).
3. This paper sought your agreement for us to work with the Ministry of Housing and Urban Development (HUD) and the Treasury to review our current funding and financing settings with a focus on:
 - a) Short-term (ahead of Budget 2023)
 - Preparing a cost pressure bid to align revenue streams with costs.
 - Confirming growth requirements for public housing beyond FY24.
 - Options for service level funding which could include funding to enable Homestar 6 version 5.
 - An extension of current appropriation funding for urban development planning, sustainability and the functions of Te Kurutao, which currently cease in FY23.
 - Preparing a bid to enable the delivery of urban development outcomes on existing land holdings outside of the large-scale projects (refer BN 22 022).
 - b) Medium-term
 - Reviewing the funding model for government housing support more generally, which could incorporate the best use of the Accommodation Supplement.
 - Developing a new funding model for public housing that better relates funding provision with the cost to deliver services.
 - Developing a model that enables our broader urban development remit in line with government direction.
4. Following advice from HUD we understand that it was decided that decisions around what aspects of this work should be progressed would be made as part of broader Budget 2023 discussions.

5. In addition, you sought further advice on a number of aspects of our briefing note to inform these discussions which this ad hoc responds to. Namely:

Accessibility

- a. Delivering an increase to the 15 percent universal design target and associated funding challenges.
- b. Gain further support from ACC and the Ministry of Health, including:
 - i. Quantifying the advantages of having accessibility interventions during redevelopment rather than retrofitting
 - ii. Discuss cost sharing for new accessible properties.

Homestar

- c. Advice around how we can measure the impact of upfront capital costs with future savings on operational costs including lower power costs and lower carbon emissions associated with Homestar.

6. The following sections seek to respond to these requests.

Accessibility

Background

7. Kāinga Ora Design Performance Requirements use three dwelling classifications that provide differing levels of accessibility support:
- **Standard:** meets typical requirements and may include universal design features.
 - **Full Universal Design:** properties considered more liveable for the entire population and are, or can be, made fit for purpose for most tenants, regardless of whether they live with a disability or illness.
 - **Accessible:** includes full universal design and additional requirements to support a particular tenant's accessibility needs¹.
8. The Kāinga Ora Accessibility Policy identifies that Kāinga Ora will deliver 15 percent of its public housing new builds to meet its full universal design standards, with the rest to meet as many as possible. This outcome aligns with Government's commitments under the Government Policy Statement on Housing and Urban Development (GPS-HUD), the Disability Strategy and the accompanying Disability Action Plan to enable homes to be liveable for a changing population. The Kāinga Ora definition of full universal design includes 36 performance indicators that must be met for a property to count toward the 15 percent target.

Review of the Accessibility Policy 2019-2022

9. Kāinga Ora is currently reviewing its Accessibility Policy, with a view that this is completed in mid-2023. The review will consider progress made against the current policy to date and identify additional areas where we consider work may be necessary in reflection of our broader mandate.
10. Additional areas we intend to explore as part of the policy review include:

¹ Kāinga Ora does not currently have a target for delivering accessible homes

- expanding the application of universal design beyond new build public housing (e.g. affordable housing)
 - incorporating a proportion of universal design into our master planning activity to support our delivery of more accessible communities
 - exploring our role in supporting more efficient delivery of housing modifications to existing homes, including implementing recommendations from our recent independent report into improving the housing modifications process.
11. We have started our engagement with the disability sector to identify what they wish to see reflected in the next iteration of the Accessibility Policy. Recommendations from the engagement process will also be costed as part of the review process.
 12. Feedback we have received so far suggests that we need to be more aspirational in our approach and aim for 100 percent universal design, given the benefits this provides to wider society. We recognise that sector expectations regarding potential increases to the current universal design target will need to be carefully managed as we move through the review process.

New funding is required to increase the 15 percent universal design target

13. The Accessibility Policy describes the current 15 percent universal design target as an 'initial' target, with the intention that this is increased overtime.
14. As the policy is now under review, there is an expectation we consider the extent to which the 15 percent target can be extended. New funding will be required to enable the delivery of any increase to the current universal design target, as this is unable to be financed through existing budgets.
15. Any increase to the current target, and funding to enable delivery, may be best considered as part of the next iteration of the Public Housing Plan noting that any decisions to increase the target would be unlikely to begin flowing into delivery for a couple of years after the decision given the time lag between commissioning homes and people occupying them.

Under current settings, the delivery of universal design is expected to become increasingly unaffordable

16. An assumption of 15 percent universal design for public housing has been built into the Kāinga Ora Long Term Investment Plan, which will see Kāinga Ora continue to deliver on its current commitment.
17. As was noted in BN 22 015, incorporating universal design at the time of redevelopment comes at a direct additional cost of approximately \$8,100 per unit. However, delivering properties that meet Kāinga Ora universal design standards often result in a trade-off in site density and cost. For example the top floors of our three level walk ups cannot be universally designed as they are inaccessible, but they have a larger footprint because the bottom floor has been designed to meet universal design requirements. This can limit our ability to maximise the yield a site would otherwise be able to achieve, resulting in reduced rental income.
18. At present, the additional expense associated with incorporating universal design and accessibility elements into our properties is not able to be recouped through higher market rents. Under current funding settings, we can expect the delivery of universal design to become increasingly expensive, particularly as Kāinga Ora continues to deliver more medium-high density developments in the future.

19. There is an expectation that Kāinga Ora will increase the 15 percent target through progressing the review of the Accessibility Policy. Estimated costs associated with increasing the 15 percent target are outlined in the table below.
20. Please note that these are high-level estimates that are intended to give an indicative view only. The table below identifies the additional cost per build to deliver universal design across a range of target increases for redevelopments. These figures do not account for other factors that further drive these costs up over the medium-long term.
21. More detailed costing work is underway to provide a comprehensive view of costs associated with increasing the 15 percent target.

*Estimated costs for increasing universal design target for redevelopments
(based on approx. 8,899 homes FY23 and FY24)*

Target	Estimated cost over and above that already budgeted for	Total number of homes over and above those already budgeted for
20 percent	\$3.56m	440
25 percent	\$7.13m	880
30 percent	\$10.69m	1320

Cost effectiveness of accessibility interventions in new builds vs retrofits

22. You requested further information on the advantages of delivering accessibility interventions at the time of redevelopment versus during the retrofit process:
- **Redevelopment** - refers to when an existing property is demolished, with the land then utilised to create additional uplift
 - **Retrofit** - refers to the process of undertaking maintenance and upgrade works on an existing property to bring it up to required standards.
23. While full universal design and accessible properties are more expensive to deliver than a standard home, incorporating accessibility and universal design features into a property at the time of redevelopment is significantly more cost-effective than doing so through the retrofit process.
24. For example, retrospectively incorporating accessibility elements into an existing property comes at a cost of approximately \$60,000 per unit, compared to an additional cost per build of \$8,100 when incorporating universal design at the time of redevelopment. The Retrofit Programmes pilot stages have identified the cost and complexity associated with delivering accessibility interventions into existing homes, particularly where the topography of a site makes undertaking this work challenging.
25. In some cases, accessibility elements are not able to be incorporated into an existing home, which requires that we move people to a more suitable property. For some customers this may mean moving to a new and unfamiliar community, impacting on their wellbeing.
26. As noted in the BN 22 015, accessibility interventions introduced through the retrofit process make up approximately 15 percent of programme costs and do not result in a subsequent uplift in rent (para 89 refers).

27. Accessibility elements have now been de-scoped from the Retrofit Programme until alternative funding sources can be sourced. The scale of this programme is forecast to reduce while new builds through redevelopment (requiring a percentage of accessibility improvements) are expected to increase.

Cost-sharing the delivery of universal design in public housing

28. Incorporating universal design at the time of a property's construction is a cost effective way of avoiding the need to fund expensive modifications at a later date, as a person's needs change over time.
29. As the Ministry of Health and ACC are the primary funders of housing modifications, Kāinga Ora considers there may be an opportunity for costs associated with delivering universal design to be shared between agencies and/or recently established Ministry of Disabled People.
30. On 19 October 2021, the Chair of the Kāinga Ora Board wrote to the Ministers of Health and ACC, noting the opportunity to consider the role housing plays in supporting the wellbeing of people with disabilities and those needing mental health support.
31. As part of this proposal, Kāinga Ora identified the reform of the health and disability system as an opportunity to introduce a more proactive model for funding housing modifications. This model would prioritise universal design and accessibility at the point of construction, rather than retrospectively commissioning and funding modifications once a property is complete.
32. Since this time, Kāinga Ora has continued to investigate whether there is opportunity for costs associated with delivering universal design to be shared and funded from these portfolios. This would see ACC and the Ministry of Health fund universal design and/or accessibility elements during the construction phase, as opposed to solely funding modifications work to existing properties, as and when specific needs arise.
33. Andrew McKenzie, Chief Executive of Kāinga Ora, intends to meet with the Chief Executive of ACC, where there will be an opportunity to discuss this further. Kāinga Ora officials also intend to meet with the Ministry of Disabled People to identify the role the new Ministry may have in supporting this work.
34. Following these meetings, we may seek your support to reconnect with the Minister of Health at a later date, given we have not yet received a response from the Ministry of Health.

Homestar

Background

35. Kāinga Ora has been using the Homestar certification system since 2019 to verify the incorporation of sustainability and wellbeing attributes within the delivery of new housing.
36. Rating tools, such as Homestar undergo review to ensure criteria are representative of current best practice, to respond to changing legislative or industry context and to improve effectiveness and/ or usability. The current version (version 5) was released in June 2022 with version 4 (which is what Kāinga Ora currently applies) expected to be retired by November 2022.
37. Kāinga Ora is in discussions with the New Zealand Green Building Council (NZGBC) to negotiate an extension to the registration cut-off date under Homestar version 4.1 to

1 July 2023 to accommodate the Kāinga Ora Public and Supported Housing delivery programme, and avoid disrupting Accelerate 24 projects. However, they are not able to extend the timeframe for use of this version beyond this date given that others in industry have already made the transition to Homestar v5. Even with this extension a minimum of 1,350 units will not achieve a 6 Homestar rating.

38. Achieving Homestar v5 would involve three key changes to the way Kāinga Ora homes are currently constructed:

- a) **Thermal envelope** - Increased insulation levels are required in the walls, ceiling and at the floor slab edge. Thermally broken windows are required to reduce heat loss. These changes are also required to meet Building Code changes which become mandatory on 3 November 2022.
- b) **Ventilation** - Mechanical ventilation with heat recovery to all dwellings.
- c) **Hot Water** - Specification of heat pump hot water cylinders instead of standard electric cylinders.

Benefits of Homestar v5

Improvement in wellbeing and economic outcomes for our customers

39. Homestar v5 also has the ability to have a significant impact on the quality of lives of New Zealand's most vulnerable. Initial analysis suggests that the changes proposed with the transition to Homestar v5 will result in:

a) **Reduced customer energy costs**

- Reducing annual hot water heating bills by ~\$700 - \$1,000 per year.
- Reducing the energy required to heat a home to healthy standards, resulting in potential energy savings of ~\$300 - \$1,600 per household (dependent upon location and energy use patterns).

b) **Improved customer health and comfort**

- Reducing the amount of summertime overheating occurring within Kāinga Ora homes.
- Reducing the level of moisture and mould within the homes, through the use of continuous ventilation systems.
- Removing allergens from the air, through filtration devices within ventilation systems.
- Reducing acoustic discomfort (for example, for apartments located on busy intersections) by allowing fresh air, ventilation and comfortable indoor temperatures without the requirement to open windows.

Alignment to Government priorities

40. Transition to use of Homestar v5 represents a single decision/ initiative that demonstrates compliance with multiple government priorities, legislative changes and programmes including:

- a) **Building Code reform** – Homestar v5 encompasses compliance with the recently revised insulation requirements under the Building Code clause H1 Energy Efficiency.
- b) **Ability to respond to additional building code requirements** - We also understand that MBIE are also considering further changes to these requirements

to minimise increase risk of internal mould and moisture issues arising from increasing in insulation levels and the Building for Climate Change Programme is proposing progressively stringent carbon performance caps to be introduced into building design and consenting processes. Homestar v5 would provide a means to respond to both of these proposals.

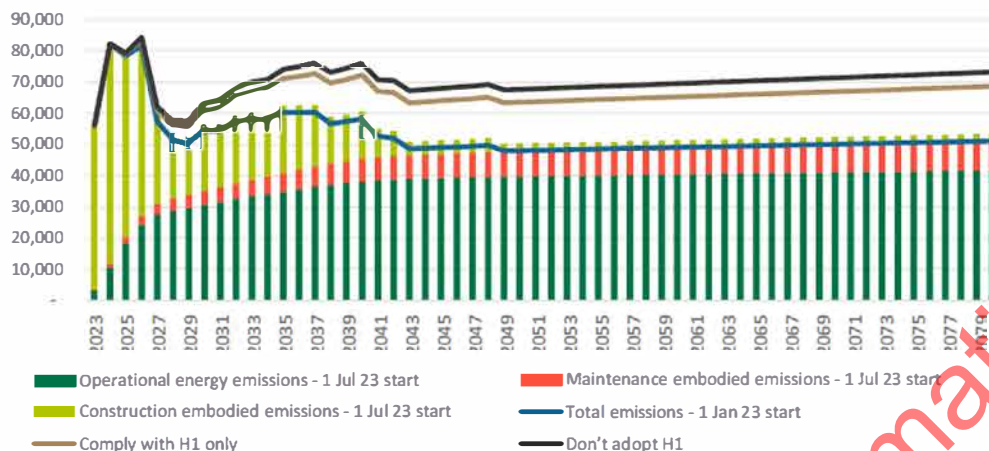
- c) **GPS HUD expectations** for Kāinga Ora to address climate change as part of delivering thriving and resilient communities.
- d) **Requirements set out in the Carbon Neutral Government Programme** for Kāinga Ora to reduce emissions by approximately 50 percent by 2030, even as the new build construction programme continues and public housing portfolio expands.
- e) **The Urban Development Act and the Kāinga Ora Homes and Communities Act** are underpinned by the need to deliver on broad outcomes including contributions to wellbeing and mitigation of climate change.
- f) **The New Zealand Government Procurement Guide** requires government projects over \$9m to select the lowest carbon option, or provide justification where this option is not selected.
- g) **The 2022 Letter of Expectation** outlines an expectation for Kāinga Ora strategy to, "include practical pathways to enable more housing delivery [...], and mitigate and adapt to climate change" and to, "please work with HUD on performance metrics" including for customer wellbeing and environmental sustainability.
- h) **Sustainable financing** – the New Zealand Government is about to start issuing Green Bonds to help raise finance for New Zealand's low carbon transition. Currently Kāinga Ora is New Zealand's largest debt issuer of Wellbeing bonds, with achievement of Homestar as the cornerstone metric used in the raising of these bonds.

Contribution to the reduction of government emissions

41. Initial analysis suggests that the transition to Homestar v5 will contribute to government emissions reductions by significantly reducing carbon emissions associated with Kāinga Ora housing (43-46 percent reduction each year over each home's life). This is equivalent to:

- a. A 100t reduction in whole of life emissions per house.
- b. A 302,000t reduction in emissions associated to our construction programme between now and 2050 and ~13,000t per year reduction thereafter.
- c. The chart below displays how delaying this transition has a significant impact on the scale of emissions reductions that are achievable. Note a few other options were considered:
 - Implementing H1 results in emissions reductions of around 77,000t by 2050 compared with continuing our current approach,
 - Implementing HSv5 as proposed results in a further 302,000t emissions avoided and reduces the carbon associated with our construction programme between now and 2050 by 21 percent
 - Bringing the transition forward by 6 months avoids a further 58,000t of emissions and brings the reduction up to 24 percent.
 - We expect any emission reductions not delivered through this transition will likely impose costs on Kāinga Ora due to the need to pay to offset these emissions.

Emissions pathway - Kāinga Ora new construction



Costs associated with a transition to Homestar v5

42. Kāinga Ora estimates that meeting Homestar v5 would result in an increase on our construction costs of about 5.4 percent across the redevelopment programme, noting that our construction cost is generally around half of the total cost of development. Attachment 1 provides a breakdown of these costs.
43. As these are costs associated with improving the performance standards of our homes. Kāinga Ora expects that this investment would be in the best interests of New Zealand from a wellbeing perspective. However, as we do not presently have an adequate funding source to enable us to proceed with it and will not directly financially benefit from the change the Board have made a decision that it cannot proceed with a transition to Homestar v5 at this time.
44. The table below sets out when costs will be incurred and the total emissions savings to and in 2050 based upon the year in which Kāinga Ora began commissioning homes to the HSv5 standard. Key points to note are:
- Emissions produced between now and 2050 are important because New Zealand has a total amount of emissions it can produce in aggregate by 2050.
 - Emissions produced in 2050 are important because New Zealand has a goal to be net neutral by 2050, emissions produced at this point will be required to be offset.

Cost and emissions implications of HomeStarv5 decision by year committed

Cost and emissions implications of HomeStarv5 decision by year committed											
Year committed	FY23	FY24	FY25	FY26	FY27	CO2 to 2050			CO2 in 2050		
	Cost (\$m)	Cost (\$m)	Cost (\$m)	Cost (\$m)	Cost (\$m)	Total (kt)	Avoided (kt)	%	Total (kt)	Avoided (kt)	%
1-Jul-22	-	3.2	35.1	89.2	45.2	1,553	396	20%	46.6	17.0	27%
1-Jan-23 (early)	-	1.8	33.7	51.9	45.2	1,587	362	19%	48.0	15.5	24%
1-Jul-23 (proposed)	-	-	2.7	33.6	45.2	1,645	304	16%	50.3	13.3	21%
1-Jan-24	-	-	1.5	32.2	26.3	1,662	287	15%	51.0	12.6	20%
1-Jan-25	-	-	-	1.4	16.4	1,717	232	12%	53.3	10.2	16%
1-Jan-26	-	-	-	-	0.7	1,750	199	10%	54.8	8.8	14%
H1 only	-	-	-	-	-	1,872	-	0%	63.6	-	-
No H1	-	(0.4)	(4.9)	(12.8)	(6.5)	1,949	(77)	(4%)	67.7	(4.1)	(6%)

Marginal abatement cost

45. The expected marginal abatement cost (per tonne avoided over 90 years) for this emissions reduction intervention is:

- a. Additional capital cost per tonne avoided: ~\$210-260
- b. Discounted value of annual additional maintenance costs per tonne avoided: ~\$100 (replacement of HWHPs and MVHR as per its expected life)
- c. Discounted value of annual energy costs saved by our customers per tonne: \$440-670 (assuming current energy cost of 30c/kwh and energy costs inflate by ~3 percent per annum)
- d. Marginal abatement cost per tonne (a + b - c): \$-130-\$-300

46. This indicates that for every tonne of emissions avoided via this investment the New Zealand economy benefits by between \$130 and \$300. This is \$215-\$385 per tonne better value than offsetting emissions at the current market price for the NZ ETS of \$85T.

47. Note that this does not include the value of other expected benefits associated with this investment which includes improved wellbeing and reduced health costs resulting from housing being warm and dry.

Funding options

48. We expect homes that meet the Homestar v5 requirements will attract a higher market rent. Assuming QV estimates are accurate (which have indicated that HomeStar homes could justify increases of approximately \$30/w more on a market rent basis) this should enable Kāinga Ora to meet the capital costs associated with the higher standards. This means that the existing funding model should automatically accommodate these improvements, however as the increased rents would be mostly met by the Crown the Crown would be indirectly paying for this.

- This has been calculated on the basis of the net present value of the future rental revenue stream that would be required to reimburse Kāinga Ora of the additional capital costs and a 2.89 percent margin (as per our target rate of return for financial sustainability).
- This varies by region as in some regions the capital costs of delivering upgrades are much higher due to climatic conditions and the resulting interventions required to deliver against energy performance targets.
- This has been stress tested against potential implications of increased whole of life maintenance costs, cost savings from avoiding buying carbon credits and potential increased costs of debt resulting from not transitioning. These may increase or reduce the required market rent uplift by +/- \$2-3 per week.

49. Should QV estimates not bear out a capital appropriation via the budget bid process (possibly via MBIE, HUD, TSY or ETS) of ~81m for the FY25, FY26 and FY27 budget periods may be required.

- These estimates have been calculated on the basis of expected additional capital costs applied to the new units in the Kāinga Ora pipeline between the periods of FY24 to FY27.

50. While this transition does not require immediate funding due to delays between decisions and funding commitments, a decision needs to be made (with some urgency) as to whether to proceed and funding surety will be required for the Board to commit to this.

Implications of not implementing this transition

51. Should the decision to transition be delayed the following implications are likely:

- a. Non-compliance with Homestar for a subset of projects risking achievement of SPE targets and the meeting of investor expectations. The NZGBC has offered Kāinga Ora some flexibility in extending use of HSv4 to accommodate our delivery programme, however they will not be able to offer this extension indefinitely. In addition, there may be reputational implications from reducing our commitment to Homestar.
- b. These homes (and their future occupants) do not benefit from the energy efficiency and wellbeing improvements that would be realised as part of Homestar v5 compliance.
- c. Homes built without adequate ventilation (particularly in high density units where the ability to cross ventilate is reduced) will be at risk of moisture issues and overheating.



Gareth Stiven
GM Strategy, Finance and Policy

Attachment 1 – Indicative breakdown of costs associated with meeting Homestar v5

The indicative breakdown of these costs by typology (inclusive of H1 improvement costs) are:

- All townhouse and standalone units to 6HSv5 – 6.4 - 7.9 percent (\$21,000-25,000)
- All apartment and walk-up units to 7HSv5 – 4.5 percent (\$21,000)

Costs also vary by region (Auckland, Wellington, Christchurch) due to different climatic conditions across the country and the interventions required to meet energy performance standards. These costs are due to:

- H1 compliance (13 percent) required to comply with building code changes
- hot water heat pump system (17 percent) which delivers hot water energy savings
- heat Recovery Mechanical ventilation (53 percent) required to ensure internal environments remain within healthy temperature and moisture ranges
- other thermal enhancements (17 percent) required to resolve thermal bridging issues.

Note: baseline is considered to be Kāinga Ora current standard practice, Homestar v4.1.

Homestar v5 requirements, costs and benefits are additional to (rather than incorporating) those associated with H1, unless cells are merged.

	H1	Homestar v5 (above H1)
Requirements	<ul style="list-style-type: none"> • Increased insulation levels and window performance 	<ul style="list-style-type: none"> • Address thermal bridging • Improved ventilation (MVHR) • Increased overall energy efficiency (Hot water heat pumps)
Costs		
Programme building construction cost uplift	0.9 percent	4.5 percent
Short term total programme costs	FY 23: \$0.5M FY 24: \$1.8M FY 25: \$12.9M FY 26: \$12.2M FY 27: “	FY 23: \$0.0M FY 24: \$0.0M FY 25: \$2.7M FY 26: \$33.6M FY 27: \$45.2M
Per unit cost uplift to implement	~\$3,000	~\$18,000-22,000
Per unit Investment Net Present Value		~\$15,000 (apartments) ~\$21,000 (standalone)
Financial BCR		1.51 (apartments) 1.63 (standalone)
Rental cost uplift req'd to fund OS/ IRRS uplift req'd to fund		~\$10-13 per week FY 2023: \$0.0m FY 2024: \$0.0m FY 2025: \$0.9m FY 2026: \$1.1m FY 2027: \$2.6m
Energy Cost Savings		
Per household % savings	~10 percent	~33 – 36 percent
Per household per week	\$5 - \$20	\$14 - 28
Per household per annum	\$260 - \$1,050	\$750 - \$1,440
Per household whole-of-life (NPV)	\$12,000	\$43,000
Carbon reductions		
Per household % reduction	~10 percent	~33 – 36 percent
Total carbon reduction to 2050	~85 kTCO _{2e}	~273 kTCO _{2e}
2050 % reduction total inventory	~6 percent	~14 percent
Benefits		
Addresses ventilation	x	✓
Addresses overheating	x	✓
Potential 2050 reduction in carbon due to influencing the sector	2.2 million tonnes	4.6 million tonnes

AH 22 083

19 July 2022

Hon Megan Woods, Minister of Housing
Cc Vui Mark Gosche, Board Chair



Further update on financial sustainability

Purpose

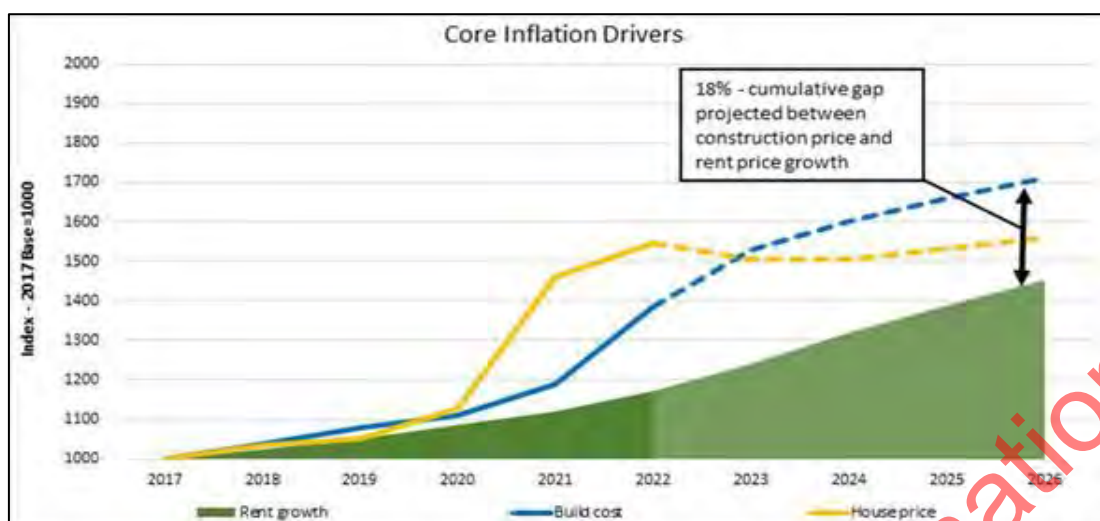
1. This advice provides you with talking points from Kāinga Ora – Homes and Communities, regarding interest in its long-term financial sustainability.

Background

2. In June 2022 we provided you with an update on the Kāinga Ora – Homes and Communities budget for 2022-26 and the implications of this on our longer term financial sustainability, in particular the impact of cost pressure and inflation and the implications of this on our funding settings, projected debt and our associated financing strategy (BN 22 015 refers).
3. This paper sought your agreement for us to work with the Ministry of Housing and Urban Development (HUD) and the Treasury to review our current funding and financing settings with a focus related to the short-term (ahead of Budget 2023) and medium term.
4. On 15 July 2022, following on from BN 22 015, we provided your office with additional information regarding accessibility and HomeStar (AH 22 077 refers).

Increasing the delivery of Public Housing

5. As stated in the proposed response to WPQ 24328 (2022), the scale of delivery of public housing achieved by Kāinga Ora is significant and it remains committed to meeting its housing supply commitments under the Public Housing Plan 2021-24, which sets out the Government's housing supply intentions.
6. Kāinga Ora has delivered a record number of houses this June – well over 650. It has also built over 8,100 newly built homes in the past five years, with the number of new state homes being built the most in two decades. There are thousands more to come as Kāinga Ora currently has over 4,600 homes under construction or contracted to be built.
7. The cost of delivering these homes, maintaining our stock has grown much more quickly than the rents we rely on to fund this activity. This is putting pressure on our operating surpluses, and is exacerbated by recent interest rate increases meaning the costs of borrowing is rising.



8. The financial position of Kāinga Ora remains strong despite the forecast operating losses. That is the cost of doing more - building more homes at scale and pace and upgrading the largest residential housing portfolio in the country.
9. Like every private or public sector business or organisation, Kāinga Ora continues to plan for and factor in the current operating environment including the costs of doing business. Kāinga Ora is exploring a number of avenues to mitigate these impacts, including reviewing plans for people growth, reassessing spend priorities that are not aligned with core delivery, continuing a major construction efficiency programme, and changes to its funding model with the Crown.

Renewing Kāinga Ora Assets

10. Kāinga Ora has a portfolio of homes that from a homeowners perspective are old, expensive to maintain; and from a customers' perspective are cold and expensive to live in.
11. Around 45,000 of our homes will be due for significant renewal (retrofit, demolition and replacement, or sale and replacement with another home) within the next 20 years. At the moment we are renewing primarily through demolishing and replacing as part of intensification.
12. The renewal programme is compressed due to:
 - the portfolio has been built up over the past 85 years in concentrated bursts of building activity
 - the differing quality of the portfolio across those bursts of activity mean some later period homes have a shorter life
 - the renewal programme started 10 years later than it should have.

Summary of variations in Kāinga Ora housing portfolio

	Pre 1936	1937-49	1950-65	1966-85	1986-00	2000+
Photo						
State houses (owned)	351	8,865	14,439	18,621	10,230	10,273
Description	Villa and Californian bungalows	Brick weatherboard. Native timbers	Brick weatherboard Native timbers	Innovative lightweight, low cost materials	Pre-modern	More modern code and specifications
Avg Asset Age	100 yrs	77yrs	63 yrs	46 yrs	30yrs	9 yrs
Indicative expected life	80-100yrs	70-90yrs	70-90yrs	40-50yrs	50yrs	50yrs
Renewal Decision Point	80-100+	70-90	70-90	40-50	50	50
Average Improvement value	\$234,000	\$124,000	\$148,000	\$177,000	\$189,000	\$265,000
Rental avg	\$590	\$407	\$406	\$423	\$445	\$487
Tenant concerns	Cold & drafty	Cold & drafty	Cold & drafty	Cold, damp	Damp	Few
Tenant operating costs	High	High	High	Moderate	Moderate	Low
Land Value: Current Market Value (2021)	0.73 Mostly land value	0.77	0.63	0.59	0.60	0.49 Mostly dwelling value
ROI (2021) Forecast	n/a	0.1%	0.5%	1.0%	1.2%	1.9%
Next Steps	Retrofit or redevelop			Upgrade & retrofit	Maintain	

Current estimated impact

Kāinga Ora renewal programme

13. The impacts of this compression of the Kāinga Ora renewal programme are:

- a concentrated and significant period of build activity, as set out in asset management plan and long term investment plan
- a more expensive maintenance programme
- debt rising quickly rather than smoothly.

14. A more optimal approach from a whole-of-life cost perspective would suggest about 10,000 homes should have been renewed by 2017. Maintenance costs for homes built pre-1970 is about \$12,000 per annum more than newer homes. While it is difficult to assess the overall cost of these delays precisely, we estimate that delaying these renewals is currently costing us around \$70 million a year. (This number would fall over time as these renewed assets begin to wear down).

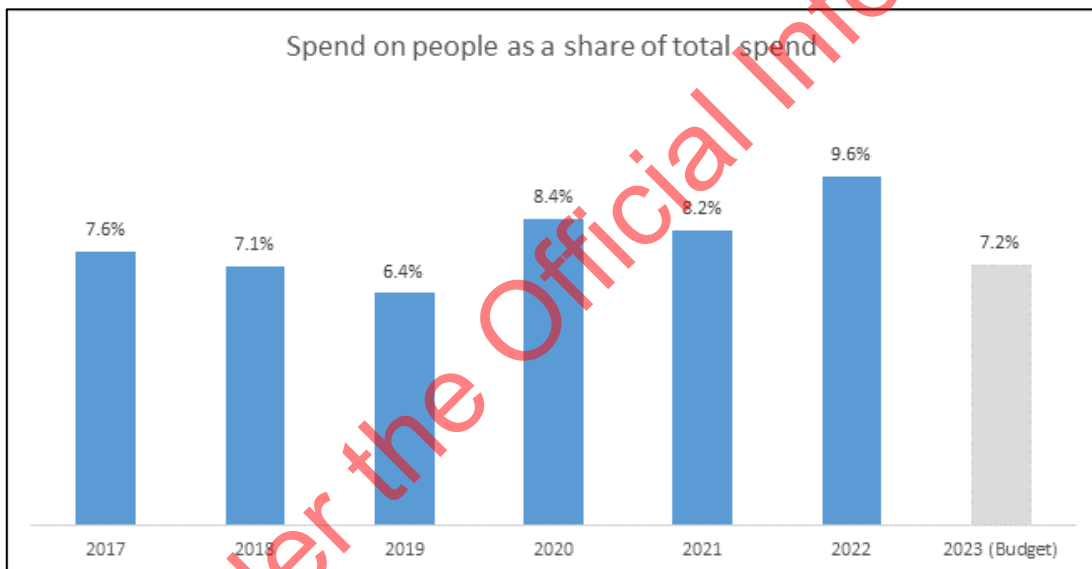
Increases in staff levels and associated costs

15. There has been a recent focus on staff growth including:

- additional roles (~200) that are supported through appropriation to take on new functions, including UD planning (which includes administering the SDP process for example), environment sustainability, broader expectations to deliver outcomes

for and with Māori, sector support programmes related to broader housing supply (KiwiBuild, HAF, Progressive Home Ownership scheme etc)

- a significant increase in the volume of work since 2017:
 - our build programme has increased from around 300 to 4,500 homes under construction
 - LSPs - in 2017 we had completed land development to enable homes on 9000 m² of land, today we have completed 80 hectares and have another 27 hectares under development, with 352 still to develop
 - an increase in the number of people in our customer facing roles so we can better support them – eg we've boosted our customer-facing team so they have more time available to support and respond to our customers, improving our ratio of front line housing support managers from ~1:350 to ~1:150.
16. On a like-for-like basis our staff costs have been very stable as a proportion of total spend. This is despite the significant service level increase associated with our Customer Programme, with an additional ~350 front line tenancy-focused staff. (Note that the 2020 and 2022 increases are associated with the capital programme being delayed due to COVID-19.)



Office costs

17. New Kāinga Ora offices were to bring people together in Wellington from three sites and in Auckland from three sites. Costs associated with the new offices included obtaining a B grade property, lease costs and refurbishment, using All-of-Government processes and at benchmarks.

Financial performance

18. Non-cash items relate primarily to achieving non-financial outcomes. Increasing housing supply and improving affordability through intensification of existing land and sale of some of that land with price and timing requirements. That has meant land is sold at below book value (including land development costs) - those book values reflect massive land value escalation over decades rather than the cost of acquisition.

Debt levels

19. Like other organisations both domestically and internationally, Kāinga Ora is facing inflationary pressures brought about by labour shortages and supply chain disruption

which has added significant costs to its build programme, and to the costs to maintain its portfolio of around 70,000 homes.

20. Kāinga Ora is also facing higher interest rates. Of note, Kāinga Ora only borrows to finance capital expenditure. Kāinga Ora borrows to pay for homes upfront, and then services that debt from the income it earns on its new homes. This is becoming more challenging as costs have increased faster than Kāinga Ora revenues.

21. It should be noted that current and projected levels of debt relative to assets, are not at all unprecedented. Throughout the 1980s Kāinga Ora (and its preceding organisations) had debt in excess of 90 percent of total assets. Debt was still above 60 percent of total in the 1990s.

Period	Average debt to asset ratio (%)
1980-1989	93
1990-1999	63
2000-2009	17
2010-2019	11
2020- forecast 2026	27

22. Looking forward, the current levels and future projections of Kāinga Ora debt and assets are as follows:

Financial Year ending 30 June 2022	FY21	FY22	FY23	FY24	FY25	FY26
Source	Actual	Provisional	Budget			
Total Assets (\$b)	40.9	49.2	51.7	56.0	58.7	61.6
Total Debt (Crown & Market) (\$b)	7.6	9.8	13.5	18.0	20.7	23.5
Debt to Assets (%)	19%	20%	26%	32%	35%	38%

Financial Year ending 30 June 2022	FY31	FY41	FY51	FY81
Source	Long term projections			
Total Assets (\$b)	70.9	82.5	104.6	260.0
Total Debt (Crown & Market) (\$b)	31.6	29.2	28.0	26.2
Debt to Assets (%)	45%	35%	27%	10%

	Actuals (\$M)			Forecast (\$M)			
	1/10/2019 - 30/06/2020	30/06/ 2021 FY	30/06/ 2022 FY	30/06/2 023 FY	30/06/ 2024 FY	30/06/ 2025 FY	30/06/ 2026 FY
Crown Debt Interest	48	49	42	69	71	69	68
Market Debt Interest	56	111	159	300	501	652	815
Total	104	161	202	369	572	721	883



Gareth Stiven
GM Strategy, Finance and Policy

Released under the Official Information Act

From: [Graham Parkin](#)
To: [EXT - David Durie](#)
Subject: Material cost increases experienced by Kainga Ora
Date: Wednesday, 17 May 2023 1:51:00 PM

Hi David

When it comes to materials, Kāinga Ora experiences general market increases via the build costs that builders/developers experience delivering redevelopments and acquire new.

(We do have National Supply Agreements (NSAs) for the maintenance programme, and negotiate prices, but often contractors have their own supply arrangements).

The information below was collated by our Supply Chain & Materials team to prepare for the negotiations of the NSAs. Below is a list of some key construction categories and the general market increases we've calculated over the past year (early 2022 to early 2023). As mentioned above, these will have been experienced by builders and developers working with Kāinga Ora to deliver new homes.

Category	General Market Increase
Plasterboard	15%
Timber	5% - 10%
Insulation	10%
Heat Pumps	6%
Vinyl Flooring	12%
Stoves and Ranges	15%
Paint	10%
Roofing	15%-20%
Hot Water Cylinders	25%

Graham

9(2)(a)

From: [Graham Parkin](#)
To: [EXT - David Durie](#)
Cc: [James Kennelly](#)
Subject: Costs and acqs and SLEDs
Date: Friday, 19 May 2023 3:04:00 PM
Attachments: [image001.png](#)
[Spreadsheet of information.xlsx](#)

Hi David

- Below is summary table of 3,000 deliveries and forecast cost and caveats
- Below that is a second table is ALL public deliveries and ALL SLEDs - the attached spreadsheet breaks this down by acquisition type and SLED type.

I'll call after I've sent through for any questions ...

From the table below -

CONSTRUCTION COST TABLE

Weighted average comes out at \$767,700

\$735,000	0.5	367500
\$760,000	0.4	304000
\$962,000	0.1	96200
		767700

Key notes to call out to Ministers Office:

- Forward cost to build estimation is underpinned by our current total development cost for Redevelopments. Excludes the cost of purchasing more land, we assume growth will be primarily delivered within existing Kāinga Ora land holdings.
- Cost is on the assumption of land to be built on is of medium quality. Risk to land conditions deteriorating (we are encountering that more often of late)
- This is a national average costing. Regions where supply & capacity is tighter will place pressure of pricing
- FY2022/23 cost benchmark reflects recent construction industry inflation pressures. Forecast escalation based on HYEPU CPI forecasts plus a premium reflecting continued price pressure in the residential construction industry
- Allowance has been made for 15% of builds to deliver full Universal Design. Accessibility not provisioned for, or additional accessibility requirements
- Build code update to H1 v5, Healthy Homes and Home Star 6 v4.1 requirements included in pricing. Home Star 6 v5 is NOT provisioned for
- Build type significantly impacts costs. Assumed 50% standard builds (stand-alone, duplex, terrace), 40% 3 level walk-up, 10% apartments.
- Price based on meeting deliveries in 2025, on top of existing PHP 2 commitments. Time delays will likely lead to further cost escalation

ACQUISITIONS AND SLEDs

Additions and SLEDs -Public homes

All Additions

Typology	01/11/17 to June-18	FY18/19	FY19/20	FY20/21	FY21/22	FY22/23 to 30/04/23	Grand Total
0 (bedsit)	-	-	-	21	-	7	28
1	145	430	424	694	259	476	2,428
2	644	622	573	814	531	687	3,871
3	249	413	244	235	325	354	1,820
4	294	406	231	277	207	216	1,631
5+	62	96	89	113	104	80	544
Grand Total	1,394	1,967	1,561	2,154	1,426	1,820	10,322

SLEDs - Excluding ICPTs

All SLED

Typology	01/11/17 to June-18	FY18/19	FY19/20	FY20/21	FY21/22	FY22/23 to 30/04/23	Grand Total
0 (bedsit)	14	8	30	34	-	-	86
1	68	62	98	86	68	103	485
2	299	215	308	314	244	188	1,568
3	239	338	310	313	272	250	1,722
4	166	76	89	89	92	89	601
5+	42	26	20	32	35	18	173
Grand Total	828	725	855	868	711	648	4,635

Additions less SLEDs

Typology	01/11/17 to June-18	FY18/19	FY19/20	FY20/21	FY21/22	FY22/23 to 30/04/23	Grand Total
0 (bedsit)	- 14	- 8	- 30	- 13	-	7	- 58
1	77	368	326	608	191	373	1,943
2	345	407	265	500	287	499	2,303
3	10	75	- 66	- 78	53	104	98
4	128	330	142	188	115	127	1,030
5+	20	70	69	81	69	62	371
Grand Total	566	1,242	706	1,286	715	1,172	5,687

Kāinga Ora Construction Costs

Introduction and Context

The following briefing provides background to Kāinga Ora led development and per square meter (per/m²) construction costs. It outlines the following core areas:

- I. Total Development Costs
 - Do Kāinga Ora developments and units cost more? And if so, why?
- II. Construction Costs
 - What is the average per/m² cost of construction for Kāinga Ora build?
- III. Costs, Benefits and Value
 - Is Kāinga Ora more expensive than the market on a per/m² basis – and if so, why?
- IV. What is Kāinga Ora doing to focus on costs and reduce them?
 - What is Kāinga Ora doing to focus on costs and reduce them?

It should be noted that the information provided mainly pertains to Kāinga Ora led development / redevelopment and not to other Kāinga Ora purchased developer led or market acquisition projects.

Each of the four sections details the following:

- **Core issue:** The main cost-related issue being addressed
- **Key Questions:** The issues rephrased as typical questions
- **Headlines:** Key responses / answers at the headline level
- **Detail:** further key information providing robustness to the main headline findings

Core Issue 1: Total Development Costs

Key Questions

- Do Kāinga Ora developments and units cost more? And if so, why?

Headlines

- It can be misleading to compare Kāinga Ora total development costs with the private developer market as there are many variables involved including land suitability, geotechnical challenges, yield, site access, locality, large scale project / urban redevelopment goals and a range of other factors to consider.
- Kāinga Ora average total development construction costs are provided below on a per unit basis and include projected price escalation out to FY25:

Typology	FY22/23	FY23/24 (10.9% price escalation)	FY24/25 (5.5% price escalation)
Standard	\$628,000	\$696,000	\$735,000
Three level walk up	\$650,000	\$721,000	\$760,000
Apartment	\$822,000	\$911,000	\$962,000
Weighted Average	<u>\$656,200</u>	<u>\$727,500</u>	<u>\$767,700</u>

- NOTES to the table:
 - The figures provided include the effects of expected price escalation out to FY24/25
 - The figures for standard houses are based on a weighted average of 97 m² of GFA and 2.5 bedrooms and for three level walk ups a weighted average of 72 m² and 1.8 bedrooms and for apartments a weighted average of 96 m² of GFA and 1.8 bedrooms.
 - The weighted average cost per dwelling above includes:
 - Land (excludes value of the land but includes getting land to build ready status)
 - Site and Civils Cost
 - Construction costs
 - Professional fees, Council fees
 - Other development costs e.g. utilities connections, development contributions
 - GST
- Comparing Community Housing Provider (CHP) costs from a dataset of approved CHP developments across the country over the last 12 months (23 developments) indicates a weighted average total development cost per dwelling (inc GST) of:
 - A one-bedroom dwelling \$486,000
 - A two-bedroom dwelling \$686,000
- It should be noted that Kāinga Ora has a range of additional challenges and constraints when developing or re-developing land, communities and neighbourhoods. Therefore it can be challenging to meaningfully compare the wide range of diverse developments that Kāinga Ora is undertaking, often with components of wider urban redevelopment, with individual private developments or registered CHP developments.

Detail

- A range of contributing variables result in a higher than average total cost of development and these include:
 - **Infrastructure / ground conditions**
 - Kāinga Ora is developing on existing landholdings and often need to remove and replace older houses as well as upgrade poor local infrastructure.
 - Kāinga Ora routinely redevelops land in existing neighbourhoods where access to sites can be problematic adding complexity and costs.
 - Historically public housing is often located on poor land where geotechnical and flooding issues persist. In most cases this requires remediation and sometimes large scale infrastructure development (e.g. flooding protection and storm water upgrade), adding time and cost to the development process. In addition, some remediation for Kāinga Ora can be of higher complexity and cost due to working to higher standards of remediation than others in industry.
 - A private developer can avoid sites where these issues of complexity and cost exist.
 - **Community facilities and parking**
 - Kāinga Ora developments provide for a high level of on-site community assets and amenity, as well as car parking in areas not required by local planning regulations. Kāinga Ora may also opt to include communal rooms and outdoor active spaces for children – features which private market developments often do not provide.
 - **Development intensity / effects on community**
 - Kāinga Ora is mindful of the effect that developments have on local communities and neighbours. This means Kāinga Ora may elect to not develop a site to its full capacity, where the impact on neighbours and communities is assessed as being too great.
 - These are constraints that private developers appear less concerned with.
 - **Engagement and consultation obligations**
 - Kāinga Ora has engagement and consultation obligations under The Kāinga Ora Homes and Communities Act 2019 that private developers do not.
 - This requires consultation and meaningful engagement with stakeholders (including mana whenua) in relation to development proposals.
 - Engagement and consultation with existing and proposed tenant communities is critical, given the effect that development can have on tenants.
 - This adds time and cost to Kāinga Ora developments that are not experienced by private market developers.

Core Issue 2: Construction Costs

Key Questions

- What is the average per/m² cost of construction for Kāinga Ora build?

Headlines

- The average per/m² cost of Kāinga Ora construction varies widely depending on a range of complicated variables that include factors such as typology, size, build and durability standards, construction methodology, and region.
- Based on the current methodology utilised within Kāinga Ora the **average contracted build cost** across all operating regions and unit typologies, is **\$3,462/m² plus GST** (based on analysis from the six months to March 2023).
- The **lowest contracted Build Cost** (in the six months to March 23) is **\$2,941/m² plus GST** in North and West Auckland, and the **highest contracted Build Cost** is **\$5,221/m² plus GST** in Otago and Southland (it should be noted that these outliers will be skewed by extenuating circumstances and therefore should be treated carefully until the full context is understood).
- Comparing national data from consent figures these show a range (based on typology) that delivers averages from Q1 2023 as follows: Stand Alone Houses \$3,075/m², Apartments \$4,710/m², Retirement village units \$2,823/m², Townhouses and home units \$2,855/m² and a total dwelling (all type) average of \$3,091/m².¹
- Based on these figures and with the caveats below noted, the **Kāinga Ora per m² cost of construction is 12% higher than the average, representing an above average mid-market range**. This is equivalent to a reasonable quality private developer (please see Core Issue 3 for a more detailed breakdown of what this additional 12% represents in respect to higher quality, longer life, amenity and size differences).
- Noting the following caveats:
 - The projects undertaken by Kāinga Ora are diverse and typology varies. There is a need to ensure that 'like with like' is being compared when external claims of build costs are being made.
 - There is no agreed and consistent methodology to build up a comparable 'per/m² cost of construction' figure in the industry – so current square meter rates that are highlighted in the media are unlikely to provide a meaningful or accurate comparison to Kāinga Ora figures.
 - Average industry construction cost rates are based on StatsNZ data and are derived from self-reported cost to build figures during the consent application process. There are advantages (reduced fees) to underreporting construction costs and therefore national average data is unlikely to yield a fully accurate picture.
- Kāinga Ora utilises their own methodology to derive comparable internal benchmarks for costs of construction across a diverse portfolio of building typologies constructed throughout the

¹ [Residential building consent analysis tables | interest.co.nz](https://www.interest.co.nz/property/123456/residential-building-consent-analysis-tables)

country. Further work is underway to compare Kāinga Ora costs to other private developers and community housing providers, but the lack of a uniform approach presents a challenge.

Detail

- Kāinga Ora Build Cost is defined as construction of a dwelling, from foundations/floor slab up. This excludes Civil & Site Works and non-construction costs (e.g. Consultants fees, consent costs, GST, etc.).
- Kāinga Ora unit typologies are Houses (stand-alone, duplex, terrace), 3 Level Walk-Ups and Apartments.
- Sample size: The headline data for the Kāinga Ora per/m² rates above is based on projects contracted over the six months in the lead up to March 2023. This represents 119 contracts delivering 364 units with a mix of unit typologies.
- An updated cost of construction from Kāinga Ora for June 2023 is imminent and this will provide additional insight in the lead up to the end of the financial year.
- Average construction cost rates from StatsNZ are based on consent application data and are linked directly to the Building Research Association of New Zealand (BRANZ) levy calculations. BRANZ charges applicants 0.1% of the contract value (above \$20,000) of every construction project applying for consent in New Zealand. As the levy, and often consenting charges, are payable by the builder, some industry experts have suggested that clients and builders may try to minimise this levy cost by inputting a cheaper cost of construction. There is potential for this to lead to stated contract values being understated, thereby reducing the accuracy of the StatsNZ data.
- In addition, the self-reported consent application data is based on predictions of cost at the start of the build process and are unlikely to account for cost increases, price escalation, overruns or contingency. In effect, it is unlikely to provide a true reflection of the final per m² cost to build.
- Using *average* costs of construction can be misleading due to the presence of significant outliers that are likely to distort the cost picture. A *median* figure may be a better reflection of typical construction costs across the diverse Kāinga Ora portfolio.

Core Issue 3: Costs, Benefits and Value

Key Questions

- Is Kāinga Ora more expensive than the market on a per/m² basis – and if so, why?

Headlines

- As stated, comparisons with national averages and quoted build costs per/m² can be misleading. Kāinga Ora houses, walk ups and apartments are more expensive to construct than basic minimum code builds and not as expensive as premium houses. Analysis of both stats NZ data and, where shared, other private developer or community housing data, indicates that Kāinga Ora builds to an approximate 'quality mid-market' cost (though it should be noted that Kāinga Ora and private developers spend on amenity in different areas – e.g. a private developer may opt to install a dishwasher where Kāinga Ora will not; whereas Kāinga Ora will install heating in bedrooms where a private developer may not).
- Kāinga Ora design requirements differ from private developers in a range of areas to cater for the needs of public housing tenants. These specific design requirements often exceed legislative controls, such as the Building Act, the New Zealand Building Code and Residential Tenancies (Healthy Homes Standards) Regulations. This results in Kāinga Ora doing things differently to the private market, particularly with respect to apartment typologies.
- Kāinga Ora specific design requirements ensure that all new properties designed, constructed, and maintained by Kāinga Ora:
 - Can be adapted for a range of lifetime needs.
 - Are fit for purpose for vulnerable people and those in need of public housing
 - Can withstand accelerated wear
 - Are cost-efficient to operate and more environmentally sound
 - Are efficient for the scale at which Kāinga Ora operates and the demand of public housing development
 - Have increased health and safety features to meet the needs of Kāinga Ora customers.
- Many of the additional features that lead to increases in initial upfront cost result in wider whole of life savings, for Customers, for Kāinga Ora and for NZ Inc. These benefits accrue and add value over the lifetime of the dwelling from improved building performance delivering lower power bills, improved health and safety, better customer outcomes, reduced building failures, reduced maintenance, as well as improving the resilience of building stock.

Detail

- Kāinga Ora builds to the needs of public housing tenants and with a long term rental investment lifespan in mind. This may result in some differences in cost per unit and in some cases costs per m² due to some of the following:
 - **Apartment dimensions** often need to be larger than private development given the mobility and universal design requirements of Kāinga Ora customers.

- Private developers typically deliver 2 bedroom apartments in the range of 59-65 m² whereas Kāinga Ora 2 bedroom apartments are typically 80 m²
- Kāinga Ora 2 bedroom apartments are as much as 36% larger than a private developer.
- The below table summarises the difference between Kāinga Ora standard apartment sizes (driven by minimum dimensions outlined in the Kāinga Ora design requirements).

Typology	Kāinga Ora – Typical Sizes	Lower Cost Private Market Developer	Percentage Difference in size
1 bedroom apartment	58m ²	42-52m ²	12%-38%
2 bedroom apartment	80m ²	59-65m ²	23%-36%

- The above differences in floor area will result in a higher cost per unit for Kāinga Ora developments when compared against lower cost apartment developers. This also means that Kāinga Ora will typically have fewer units on the site than a low cost market developer may. In some instances Kāinga Ora will have fewer overall units per floor in order to appropriately manage Kāinga Ora public housing customers. This results in the common area costs, amenity and in ground costs being spread across fewer units and thereby leading to increased overall costs per unit as well as proportionately increased per dwelling costs/m².
- **Lifts / Services**
 - Kāinga Ora customers typically have higher mobility requirements so need more lifts than a private developer
 - **Homestar / Healthy Homes / Innovation**
 - Kāinga Ora has previously committed to delivering all new developments to a minimum of 6 Homestar, and increasingly achieving some developments at 7 and 8 Homestar. This delivers a range of environmental benefits as well as increasing overall water and energy efficiency, delivering less expensive ongoing bills for Kāinga Ora customers.
 - The average cost of delivering 6 Homestar (v4.1) is \$127/m² [based on a 2 bedroom unit].
 - Kāinga Ora is also working towards the prescribed government goal of being carbon neutral by 2030. This includes exploration of pilot programs related to construction innovation, such as applying mass timber construction and low carbon concrete build methodologies.
 - Kāinga Ora made a commitment to be early adopters to the recent upgrade in NZ Building Code clause H1 dealing with energy efficiency – spending more to deliver a higher performance thermal envelope, lower energy bills for customers and greater whole of life value.
 - Private market developers have no obligation to deliver developments achieving 6 Homestar or above, nor to drive innovation in order to reduce carbon emissions; and most have opted to adopt higher standards set out in the recent Building Code updates only when legally required to do so.

○ **Universal Design and Accessibility**

- The cost of incorporating full Universal Design (fUD) features depends on bedroom typology – this adds approximately \$64/m² plus GST [based on a standard 3 bedroom unit]. A Kāinga Ora 3 bedroom unit is roughly 115 m² GFA and therefore total extra cost is approximately \$8,500 per 3 bedroom home.
- The cost of incorporating accessible features depends on bedroom typology – this adds approximately \$128/ m² plus GST [based on a standard 3 bedroom unit]. Adding in the region of \$17,000 for a 115 m² 3 bedroom home
- If the GFA (Gross Floor Area) of a unit needs to be increased to accommodate fUD/Accessible features, this can add up to \$734/ m² plus GST [based on a standard 3 bedroom unit]. Much of this is reflected in a reduced on-site yield (fewer but larger apartments and potentially fewer apartments per floor). This would add in the region of \$97,000 for the 3 bedroom 115 m² example used here.

○ **Amenity, comfort, safety and durability**

- Many Kāinga Ora customers spend more time at home than the general population and therefore Kāinga Ora is cautious about reducing overall amenity to gain site efficiency (e.g. provision of smaller living sizes, or reduced daylighting into second bedrooms).
- Kāinga Ora installs a range of additional beneficial features that are not common to all private developments including heat pumps in living rooms, heaters in bedrooms, curtains throughout, smoke alarms in all bedrooms, minimum of two toilets in 3 bedroom homes, baths as well as showers, stainless steel benchtops, clothes lines, lockable outdoor storage, larger outdoor balconies, security lighting and CCTV systems, shared communal spaces.
- Kāinga Ora ensures compact, people-centred design in their higher density developments. Multi-functional community rooms, including kitchens, tenancy management offices and open plan spaces are typically incorporated. Shared green spaces and children's playgrounds also enable residents to connect with one another and encourage wellbeing. Careful consideration is taken towards landscaping, which often includes native plants/shrubs, citrus and specimen trees.
- Kāinga Ora is aware of the need for homes to be robust, easily maintained and durable. This is especially important given the number of houses owned by Kāinga Ora as well as the challenges for moving customers out whilst repairs are undertaken. This requires a level of upgrade to some fixtures and fittings e.g. kitchen cupboards are routinely attached with three hinges instead of two, solid core doors and durable commercial grade vinyl are used, vandal resistant common area lighting and tamper proof electrical boxes are provided.
- A number of the design and construction requirements outlined above also have an impact in terms of a reduced yield on a site. Kāinga Ora makes provision for car parking, separated driveways and footpaths, CPTED features (crime prevention) and wider access ways – all of which increase amenity, health, safety and security but also increase overall unit and cost/m² price.

Core Issue 4: Reducing Costs

Key Questions

- What is Kāinga Ora doing to focus on costs and reduce them?

Headlines

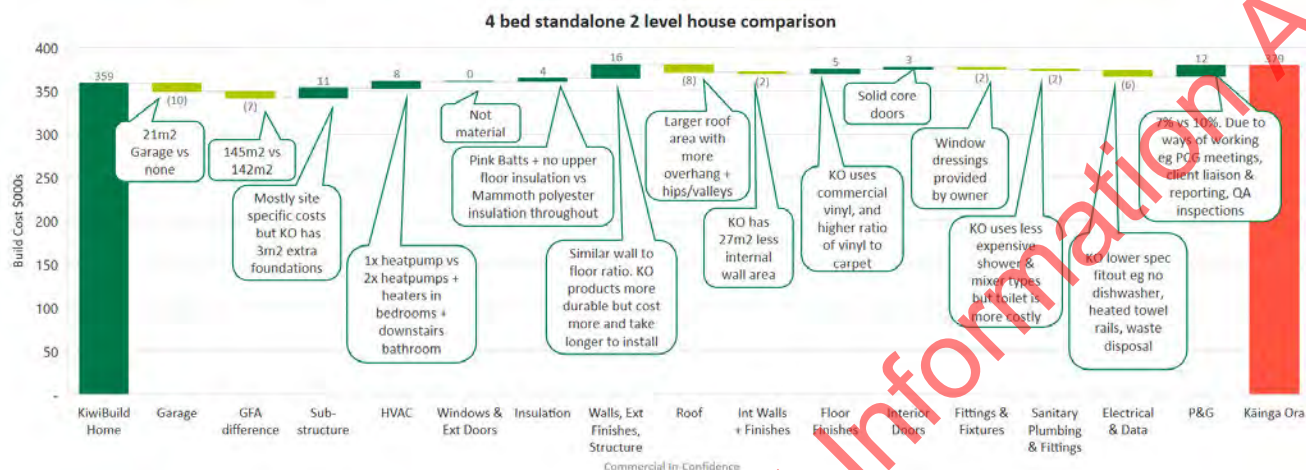
- As an agency with one of the largest asset bases for the Crown, Kāinga Ora takes a long-term fiscally responsible view to managing the housing portfolio.
- Kāinga Ora cost increases compared to market increases in recent periods have been well managed. The change in Kāinga Ora average build cost / m² comparing (Jan to Aug 2022 : Sept 2022 to February 2023) represented a 6% increase
 - This is significant achievement when compared to the producer's price index which was up 11.8%, or Core Logics Cordell's Construction Cost Index cost to build 3 bedroom home in 12 months to December 2022 up 10.1%².
- Kāinga Ora is focussing on cost reduction in a number of key areas including driving waste and inefficiency out of construction through a new Housing Delivery System (HDS), innovation utilising more Off-Site Manufacture, continual improvement looking at more efficient floor plan design and work on National Supply Agreements to deliver cost reductions on standardised items.
- Kāinga Ora has a team of Quantity Surveyors and financial professionals who monitor cost performance against internal rate benchmarks, industry standards and best practice to ensure Kāinga Ora is getting, and delivering, value.
- As part of a Spending, Funding and Financing Review, Kāinga Ora is implementing a programme of work benchmarking developer-led projects against Kāinga Ora-led projects and analysis and reporting is underway.

Detail

- Kāinga Ora is focussing to improve how they work and deliver more quality homes faster.
- The Delivery Transformation Group is improving the way Kāinga Ora works through the development of the Housing Delivery System (HDS)
 - Subject to market rates, Kāinga Ora has set an ambition to drive cost savings through increased productivity, material savings and reduced overheads which could be up to \$82,100/home when the system is fully embedded and optimised. Cost savings will be more firmly quantified once there have been more housing units delivered.
 - Pre-Construction time savings - depending on sizes and locations HDS Projects are averaging 35 working days (49 calendar days) for the pre-construction process, compared to standard time of 523 days.

² Source 1: Statistics NZ, Producers Price Index (Outputs), Building Construction for the period Jan to Dec 2022 – Cost increase 11.8%. Source 2: Property research firm Core Logic's Cordell Construction Cost Index (which measures the cost of building a 'standard' three-bedroom brick and tile house) for the period Jan to Dec 2022 – Cost increase 10.1%

- Comparison benchmarking work utilising specific data from private developers is underway and is yielding pertinent findings. The example below presents a bridge diagram that compares a fairly typical 4 bed two level KiwiBuild design to a Kāinga Ora Standard plan and highlights the differentials of cost between the two; with the typical KiwiBuild home costed at \$359,000 compared to the Kāinga Ora home at \$379,000. This analysis highlights the impacts of additional Kāinga Ora specifications and requirements.



- The comparison above includes build costs only. It excludes civils, demolition & site work, utility connections, build & development margins, financing etc.