



Governor

Prices, Regulatory Affairs & Special Projects Division
Received 24/09/09

Bank of Papua New Guinea

To Robert Haus
Douglas Street
G. P. O. Box 121
PORT MORESBY
National Capital District
Papua New Guinea

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22 September 2009

Office of the Commissioner
Received 24/09/2009

Mr. Thomas Abe
Office of the Commissioner & CEO
Independent Consumer & Competition Commission
1st Floor, Garden City
PO Box 6394
BOROKO
National Capital District

Dear Mr. Abe,

RE: HOUSING INDUSTRY REVIEW

I refer to your letter of 11 August 2009 seeking comments on the Issue Paper on the above subject matter.

In 2007, I provided a comprehensive assessment and recommendation on the proposed National Housing Policy which covered some of the issues you requested stakeholders to comment on. A copy of my submission to the National Housing Policy Taskforce chaired by the Secretary for Treasury, Mr. Simon Tosali, is attached for reference. It is my strong view that the issues raised in this submission are still relevant for the purpose of the current review by the ICCC.

Yours sincerely,

Sir Wilson L. Kamit Kt, CBE

....attachment.

06 November 2007

Mr Simon Tosali
Secretary, Department of Treasury, and
Chairman, National Housing Policy
4th Floor, Vulupindi Haus
P.O Box 710
WAIGANI
National Capital District

Dear Secretary Tosali,

RE: NATIONAL HOUSING POLICY

I refer to your letter dated 13 August 2007 inviting the Bank of PNG to make suggestions for a National Housing Policy.

Following consultations with stakeholders, including the banks, developers and other interested parties I wish to outline a general framework for a National Housing Policy.

The shortcomings of the existing structures, programs and schemes put in place were that, they catered to a specific employer, be it in the private or public sector. What was and still is missing in all of the existing schemes is the catering to the general public's need for housing. Those fortunate to belong to a favoured group, like public sector employees or a private sector employer that saw an advantage to provide housing to their work force benefited, while the great majority were left out.

One of the main faults of the existing policies is that it never attempted to deal with the so called illegal settlements that mushroomed in the major urban centers, and run down urban neighborhoods that turned into slums.

The other shortfall of the existing policies were that, they limited the discussion to residential buildings, it shied away from office, other buildings and structures owned by the different levels of Governments - National, Provincial, District and Local. In the cases where the National Government has full ownership and control the Policy Paper should provide a clear implementation plan, in the others a recommended way of action could be outlined.

This policy paper will be divided in two main parts:

1. Buildings and Structures Presently Owned by the Government.
2. A National Residential Housing Policy.

1. Building and Structures Presently Owned by the Government.

The experience in the thirty two years of independence showed that, the conditions of Government owned office buildings, residential housing and other public buildings and structures have deteriorated to such a bad state reflecting a total failure by the Government in maintaining them to a minimal acceptable standard. The result is that many of them deteriorated to such an unusable level and were abandoned. E.g. Pineapple building). Others are in a state of disgrace - elevators don't work, broken doors and windows, toilets and sanitary conditions that any independent assessor will declare them as unhygienic and a health hazard. It is clear that, governments at all levels, in the great majority of the cases fails to maintain its buildings, houses and other structures at an acceptable standard.

There is no difference between governments owned houses, buildings and structures and those placed into the custody of a government owned and managed corporate entity like the National Housing Corporation. In the later case, in addition to the maintenance problem, the experience in developed as well as developing countries is, of delinquencies of rental payments, favoritism in allocation of houses and space, political cronyism, gross inefficiencies in operational and financial management, abuse of trust, misappropriation of funds, and existing outright theft were rife.

In my view the solution is to tender for sale all existing government buildings, structures and houses. The proceeds received for the sale, or an indefinite lease, should be placed into a Sinking Fund to be used for the sole purpose of renting or leasing the buildings and structures the government needs for its operations. The rentals and leases can be for the useful life of the buildings and structures for all practical purposes it is an indefinite life span. The rental, or lease agreements must define a very high standard of maintenance which if not adhered to, will result in the agreement to be discontinued and in cases that the State is bound to have the use of the building and/or the structure be forfeited at no cost to the Government. One example of the later will be hospitals, classrooms and aid posts or the official residence of the governments at all levels must provide, such as the Governor General's or Prime Minister's official residences. For this arrangement to be workable, very detailed renovation and maintenance schedules will have to be developed and incorporated in all rental and lease agreements and very strictly enforced.

It is a multibillion kina out sourcing plan that has to be very carefully designed formulated and implemented. There is not and there will not be sufficient resources in the private sector to implement it simultaneously for all the Governments

buildings, houses and structures. The government should develop a list of priorities and a ten year implementation program by which time all the buildings, houses and structures used by the government at all levels will be rented or leased.

The externalities of the program are immense. It will enhance the development of a strong local construction, real estate, building maintenance and very long term mortgage finance industries. Those industries were the backbone of economic and industrial development in most (if not) all the developed countries. It will reshape the labor market, the construction and the manufacturing industries. The private sector will be able to reinvest all its earning and accumulated resources in the domestic economy at a very reasonable return. Governments will overcome the major impediment it is facing of maintaining the buildings, houses and structures it invested mammoth resources in the past at acceptable and useable standards.

In the short term, it might be seen as an increase in the recurrent cost of running the government operations, although the income generated from the Sinking Fund should be substantial. In the long term, it should result in substantial savings in the recurrent cost, taking into account the pace at which some of the major buildings occupied by the National Government will come under the axe and declared unsuitable for use. The Pineapple building is already there, the Old Government House and others are reaching the same state at a very fast pace.

The treatment of the buildings, houses and structures owned by governments is closely related to a National Housing Policy. The interrelation is through the overall development of the construction, real estate and mortgage industries. A relatively large market for new construction, renovation, maintenance and rentals of office space for the Government by the private sector, will enable it to undertake the opportunities and risks involved in solving the housing problems of households in the urban centers.

2. A National Housing Plan (Policy)

The term "plan" should be preferred to the term "policy". The policy can be defined in a few words, which should say ". The State Must Create the Enabling Environment for All Papua New Guinean's to Have Decent and Hygienic Accommodation at an Affordable Cost". The plan should detail, how it can be achieved, what has to be done and the mile stones.

There are three basic parameters that should be looked at:

- (1) Availability;
- (2) Affordability; and
- (3) Financing.

Most of the discussion held in Papua New Guinea have been concentrated on the third parameter, funding (Mortgage Financing), of housing schemes developed by

public and private, sector employers the Government owned Housing Corporation, superannuation funds and occasionally a developer that managed to get a site such as the Rainbow Estate in the suburb of Gerehu in Port Moresby.

What this paper will attempt to do is to put forward a plan that should deal with the issue of anyone in need for housing. We all know that it is a continuous problem that will be with us for the foreseeable future.

(1) Availability

The discussion on availability will deal with the Land, Infrastructure and Construction.

- a. The provision of land for housing development is the responsibility of the National and Local Level Governments. Once the land is identified it is the National and Local Level Governments that have to unconditionally commit that basic infrastructure of road, water, sewerage, electricity and communication to the site is provided.
- b. In this regard the National Housing Corporation that sold all its existing houses and structures as proposed above, can play the role of identifying the land and have the role of securing that the infrastructure developments to the site is implemented.
- c. The land should be tendered in an open competitive fashion by publishing it in at least two English and one Pidgin language news papers, and the National Gazette.

There are three options that will be presented:

- (i) The land is State or traditionally owned and the houses are to be sold on the open market at the going market price.

The principle applying to the tender should be the neighborhood development plan as per the zoning of the area by the Town/City Building Board. All public buildings including those to be used by the Government or shopping centers (Malls) should be part of the land tendered to the developer, and clearly defined in the master plan. The Town or Municipality Building Board should ensure that it fits the Overall Town Development Plan and the Specific Plans of the neighborhood the housing scheme is going to be built in.

If the site includes public buildings and structures such as schools, health centers, police stations for example, the developer will commit to build them and lease them on the same terms and conditions such buildings and structures are leased as presented above. The impact

this will have on the price of the houses see the affordability discussion below.

(ii) Renovation of a slum.

We define a slum as a run down housing site occupied legitimately by those living in the houses. The existing houses can't be renovated, are a health hazard to the occupants and have to be torn down and rebuilt.

The National and Local Level Governments to negotiate with the community on the renovation of the neighborhood and resettling of the existing occupants.

The Town/City Building Plan should take into account the resettlement program, make allowances for it in the utilization of the land for housing.

The way it should be done is, the area to be rezoned to a higher density zoning by allowing the developer to free up land to be sold on the open market. The Town/City carries out a valuation of the project to make allowance for the cost of resettling of the slum occupants to be paid for by the area the developer can use constructing public buildings and structures to be leased to the National and Local Level Governments, shopping centers and malls and houses to be sold on the open market. In most checked cases of rehabilitation and resettlement of slums the occupants did not have to pay for their new apartments. In almost all instances the area was rezoned from single to multi story buildings, substantial areas were assigned for trade and public buildings and structures. The rezoning should make the projects economical to the developers and no direct subsidies should be provided.

The land should be tendered to developers in an open tender. The valuations should be fully disclosed in the tender documents. The developers should be asked to comment and if any changes are introduced all those submitting tenders must be informed.

(iii) Solving the problem of illegal settlements.

We define a Settlement as a group of people residing illegally on land the owner of which is known. The owner of the land and the enforcement agencies of the State and/or the Municipality can do nothing or very little to remove them and protect the rights of the lawful owner.

The cost of providing housing to illegal settlers is very high. It involves, paying for the land to the landowners, developing the land and infrastructure, constructing the houses, resettling the illegal settlers and selling the rest on the open market.

To turn a resettlement project even marginally economical, the buildings and structures leased by the National and Local Level Governments have to be very substantive, the zoning to allocate large tracts of the land for commerce and trade and the cost of the land to be low. The latter is less of a problem.

The landowners will realize at least some income compared to none if the project is not implemented.

The area will have to be rezoned to very high density occupation with high rising buildings, large allocation of land to public buildings and structures commercial and trade usage like shopping centers and malls.

Settlers will rarely have the capital to buy the apartments or housing units. Most of them will be casually employed and will not qualify for a mortgage.

One of the solutions used in many countries is a lease purchase option at the tenant's discretion.

(2) Affordability

The affordability issue is dealt with through:

- a. Rezoning of the area and moving into high density construction, multi story buildings, as more costly the solution the density to be increased.
- b. In the process of rezoning there is an allocation of land to construct buildings and structures for commerce and trade. The developer can recover a substantive part of his investment by selling or leasing them out. As more costly the solution a higher proportion of the land is allocated to this use.
- c. The allocation of land for public use by the National and Local Level Governments and their commitment to lease the buildings and structures for an indefinite time, provides the developer an immediate secured very long term cash flow on the completion of the project.

- d. This combined with the flows of (b) above should allow the private entrepreneur, developer some breathing space to carry out the sale or lease of the apartments and units constructed.

(3) Financing

- a. The developer will agree with a bank or financier on funding the mortgages of the project. The standard funding arrangements known are that the developer agrees with the bank on an interim financing arrangement to be used as working capital during the planning and construction stage. The future tenants, that choose to have a mortgage loan, will be entitled to get it, if they conform with the terms and conditions agreed between the developer and the bank, like an employment and income test, or any other criteria agreed between the bank and the developer. The maximum amount (percentage) of the cost to be funded by a mortgage loan is agreed between the bank and the developer, the amount the tenant will be entitled to, is decided by an income test.
- b. The equity portion is paid by stages during the construction period as agreed between the tenant and the developer. It is the practice that the equity payments are proportionate to the progress of the specific building or unit the tenant purchased. It is standard practice that ten percent (10%) of the total price to be paid on completion and the transfer of the rights to the apartment or unit to the tenant.
- c. The superannuation funds are long term saving institutions pension type schemes that should provide income for retirees and their families. As such, the accumulated savings by contributors should not be used as housing loans to the members. Such uses reduce the rights on retirement or the entitlement of the families if the member is deceased.

The way the superannuation funds can participate in financing is by direct investment as an entrepreneur shareholder in the project. As a substantive shareholder it will be in position to influence the cost and the terms to the buyers of the apartments or the units at large and to its contributors specifically. There are many ways this can be done, and will not elaborate on it in this submission. It will be discussed between the Bank of Papua New Guinea the regulator and the superannuation funds on a case by case basis.

The other way will be by providing the banking system long term savings, in the form of deposits or bonds to fund the long term mortgage loans. This will allow the banks to extend the term of the loans and increase the share of the cost funded by the mortgage. As

presented above the percent of the cost funded by a mortgage has to pass the repayment capacity test. The longer the repayment period, the percent of the cost funded by a mortgage can be higher.

- d. As mentioned briefly in the discussion on the sourcing out of all Government owned buildings, houses and structures it will have a great impact on the mortgage financing industry. The need for long term funding will increase and become very large. The providers of the mortgages should be the banks and finance companies. The source of the funds is the superannuation and life insurance industries that are long term saving schemes. In many countries the banks and finance companies offered longer term saving schemes to fund their mortgage operations.

In this submission I tried to present a comprehensive housing development plan. The basic paradigm is that we base it on a Master Municipality (city, town or village) Plan which deals with the zoning and if needed rezoning of the neighborhood, including the construction of public buildings and structures, commerce and trade needs for those that will occupy the area and the neighborhoods surrounding it.

The submission deals with construction for the public sector, including the solution of the existing buildings and structures owned by the National, Provincial and Local Level Governments, the future needs of the public sector and the interaction between them and how it can support the need of housing by households that can afford to pay the full price and those living in slums and settlements that have to be assisted to purchase or rent their accommodation. The assistance is through the use of a fair, unbiased economic mean of rezoning, public buildings and structures and commercial sites of shopping centers and malls.

I started with the sourcing out of buildings, houses and structures used by all levels of Government. This is the base which will enable the private entrepreneurs, developers becoming the main actors in solving the housing problem of the nation. I also highlighted the impact it will have on the mortgage financing industry.

The Bank of Papua New Guinea is willing to assist in any way possible in developing a comprehensive, economically viable, long term National Housing Plan. One possible option is outlined in this submission.

Thank you for inviting the Bank to contribute.

Yours sincerely



L. Wilson Kamit CBE