



Financial and Fiscal Commission Local Government Fiscal Framework and Housing Finance Public Hearings

Presentation to the Portfolio Committee on
Cooperative Governance and Traditional Affairs

08 May 2012

Presentation Outline

Introduction

1. Local Government Fiscal Framework Public Hearings

- 1.1. Background to process
- 1.2. Structure of 1st public hearing
- 1.3. Outcomes of 1st public hearing
- 1.4. Way forward

2. Housing Finance Public Hearings

- 2.1. Background to the process
- 2.2. Discussion of stakeholder perspectives on housing challenges
- 2.4. Research gaps identified

Introduction

- FFC has legislative mandate to make annual recommendations for DOR
 - Constitution
 - IGFR Act
 - Money Bills Amendment Act
- FFC Act further empowers Commission to actively engage in current policy debates
 - Mandates Commission to take own initiatives
 - Ensures independent view

Benefit of Public Hearings

- Commission's interaction with stakeholders
 - Generate research and recommendations through comprehensive and extensive public hearing processes
 - Develop recommendations through a process of partnerships and interactions with the role players in the system
 - Will complement the broader work and mandate of the Commission
- Advantages of public hearings
 - Improves interaction with stakeholders
 - Allows Commission to understand needs of key stakeholders
 - Allows for a forum for all ideas and viewpoints to be debated
 - Obtain a consensus from all stakeholders on policy and research issues



1. Local Government Fiscal Framework Public Hearings



1.1 Background

Why LGFF is Important

- LG sphere continuously evolving
 - LGFF needs to be robust to cater for changing needs of LG
- To be sensitive to various needs of municipalities
 - Urban/rural dimension
 - Balancing urban built environment needs with rural development
 - Increased urbanisation
 - Increasing devolution of powers and functions
 - Poor municipal expenditure and revenue performance
 - Poor coordination and support between and amongst spheres
- Are municipalities appropriately funded and capacitated?
 - Continues to hide non-fiscal problems
- Complements government wide initiatives to review LGFF

The Public Hearings Process

- 1st public hearing
 - Outline problem statement
 - FFC compiled a problem statement discussion document
 - Presented retrospective overview of LGFF and highlight key issues for debates
 - All stakeholders were requested to present own views on LGFF and methods to improve it
 - Consensus on set of research questions and the general problem statement
 - FFC undertaking research on issues raised
- FFC to hold 2nd set of hearings in 2012



1.2 Structure of First Public Hearings

General Proceedings

- 1st hearing was jointly hosted by the FFC and the Limpopo Provincial Government
- Hearing held in Polokwane on 03-04 October 2011
- 1st day included presentations from stakeholders
 - Offered national, provincial and municipal views
 - Laid out the funding constraints faced by different municipalities
- 2nd day breakaway groups and discussions focused on:
 - LES and conditional grants
 - Municipal own revenues
 - Intergovernmental fiscal coordination
 - Differentiation of municipalities

Range of Stakeholders in Attendance

- National departments
 - National Treasury
 - DCoG
- Provincial governments
 - Treasuries and local government departments
- Local Government
 - SALGA
 - Metros
 - Smaller/rural municipalities

Range of Stakeholders in Attendance

- Legislature
 - Members of parliament
 - Members of provincial legislatures
 - Councillors
- Other
 - Academics
 - World Bank
 - Public Service Commission

Key Questions/Issues for Public Hearing

- Is current LGFF catering for needs of all municipalities in the country given their unique characteristics?
- What factors inherent in the current policy and fiscal environment hinder appropriate funding of municipalities?
- Is current legislative framework governing local government fiscal matters impacting negatively or positively on municipal performance?
- What issues in LG and IGFR systems weaken the performance of municipalities?

Key Questions/Issues for Public Hearing

- Does fiscal framework achieve appropriate balance between equity concerns and promotion of good governance?
- Are current revenue instruments afforded to municipalities sufficient, well designed and appropriately implemented?
- Is current LGFF robust and dynamic to cater for evolving sphere?
- What other aspects should be catered for in LGFF?
- What changes or improvements should be factored in LGFF?



1.3 Outcomes of 1st Local Government Fiscal Framework Public Hearings

Stakeholder Response on Issues

- Principles of differentiation agreed upon but basis is contested
- Views on LES
 - Call for a review of vertical and horizontal division of revenue
 - Conduct a transparent review of all LES formula components
 - Update data for improved insight into demographic profile of municipalities

Stakeholder Response on Issues

- Views on conditional grants
 - Highlighted challenges associated with a plethora of conditional grants
 - Capacity support to accompany conditional grant allocations where necessary
 - Recognise and reward performance
- Views on municipal own revenues
 - Fair evaluation of financial constraints in both urban and rural areas
 - Review true own revenue sources and their regulation
 - Have a social compact over service delivery

Stakeholder Response on Issues

- Views on other issues
 - Local government challenges require a whole-of-government response
 - LGFF review should be informed by a review of the institutional framework
 - Municipalities are facing increasing cost pressures

Principles to Guide FFC Research

- Better understanding of dynamic between fiscal capacity and fiscal effort needs to inform any revision of the fiscal framework
- LGFF should ensure that incentives created in the IGFR system are compatible with policy intent
- Fiscal criteria for re-demarcation should be clarified
- Design of a new LGFF must be predicated on a clear understanding of redistributive and growth-enhancing roles of local government

Principles to Guide FFC Research

- Core dimension of LES as an unconditional equalisation grant
 - Need to be dynamic
 - Allocations need to be adequate and sensitive to powers and functions, expenditure needs, revenue adequacy and cost disabilities
 - LES should align with developmental role of LG in addition to Constitution requirements
- Backlogs should be taken into account explicitly in determining the LGFF

Principles to Guide FFC Research

- Inadequate policy coherence and lack of implementation support from national government have exacerbated dysfunction within the local sphere
- Conditional grants are supposed to trigger behaviour change in order to engender outcomes
- Instead of focusing on categorisation into urban and rural municipalities, focus should be on the linkages between urban and rural areas within functional economic regions
- All elements of the LGFF should be transparent to all stakeholders

Research Gaps Identified

- Costing of basic services
- Understanding fiscal capacity and fiscal effort
- Optimal allocations and design of fuel levy sharing mechanism
- Impact of demarcation process on municipal fiscal capacity and sustainability
- Understanding municipal allocative and technical efficiency

Research Gaps Identified

- Review of regulatory framework for municipal tariff setting
- Understanding cost of reporting compliance
- Optimising property rates revenues
- Process of effectively differentiating municipalities
- Municipal borrowing: principles and challenges

Research Gaps Identified

- Maintenance and rehabilitation of municipal infrastructure: funding models and incentives
- Defining, measuring and rewarding municipal performance
- Identifying data gaps at municipal level



1.4 Way Forward

Way Forward

- Further research will be undertaken to inform an FFC options analysis
 - Based on FFC principles
 - Inform options and recommendations for FFC
- Options analysis report and FFC recommendations to inform second public hearing
 - Proposed for 4-5 June 2012
- Align research gaps to FFC research agenda



2. Housing Finance Public Hearings



2.1 Background

FFC Programme on Housing Finance

- Concerned by evidence of real challenges in housing delivery system and financing model
 - Mismatch between growing demand and supply capability
 - Protests related to delays, quality, location, fairness
 - Growing fiscal burden in a period of austerity
- FFC focussing its work on housing finance:
 - Deepen analysis of human settlements challenges
 - Develop special (“out of cycle”, long term and systemic) recommendations
 - Provide a platform constructive interaction between stakeholders
- First round of public hearings
 - Held on 13 - 14 Oct 2011 in Ekurhuleni, with stakeholders making extensive submissions (see www.ffc.co.za)
 - Focused on analysis of the problems and challenges, not solutions
 - Not a traditional FFC research instrument: action oriented and consultative



2.2 Discussion of Stakeholder Perspectives on Housing Challenges

Stakeholder Perspective on Housing Challenges

- a. Insufficient scale relative to demand
- b. Fiscal and physical sustainability
- c. Household affordability
- d. Informality
- e. Barriers in the delivery chain (land, infrastructure, zoning, registration in deeds, etc)

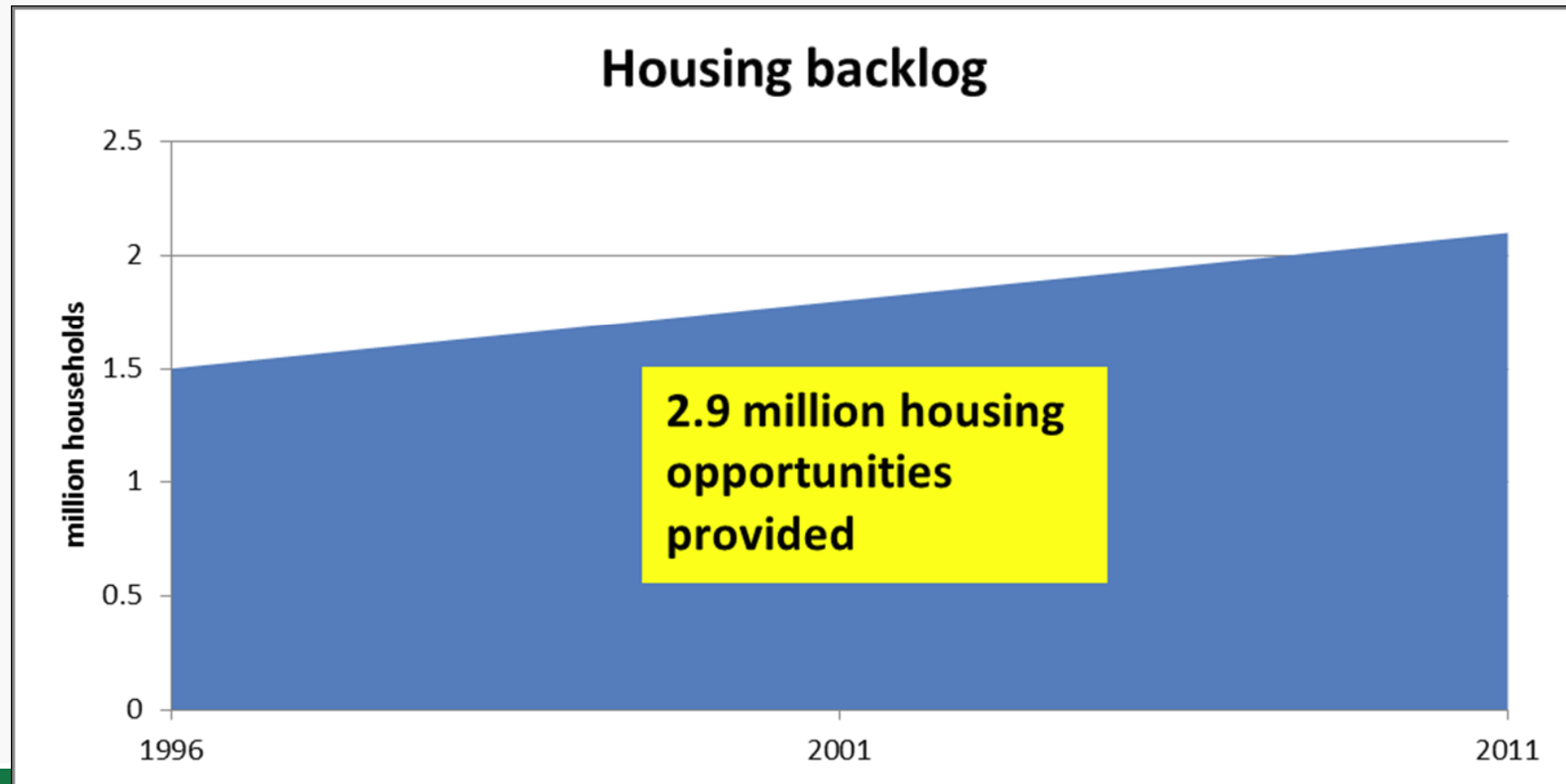
Stakeholder Perspective on Housing Challenges

- Generally, stakeholders agreed with the FFC starting points
- Stakeholders emphasised the following points as concerns:
 - **Policy flexibility versus implementation rigidity**
 - While national policy gives provincial and local governments the flexibility to adapt housing policy and plans according to their context, stakeholders perceived national government as dictating a “one size fits all” approach
 - **Legislative and administrative barriers in the housing market**
 - Include limited accreditation of municipalities to perform housing functions (Housing Act)
 - Regulatory constraints (MFMA) prevent metros using own revenues as bridging finance for low-income housing developments
 - DFIs not providing significant bridging finance to metros: legislative change may be required

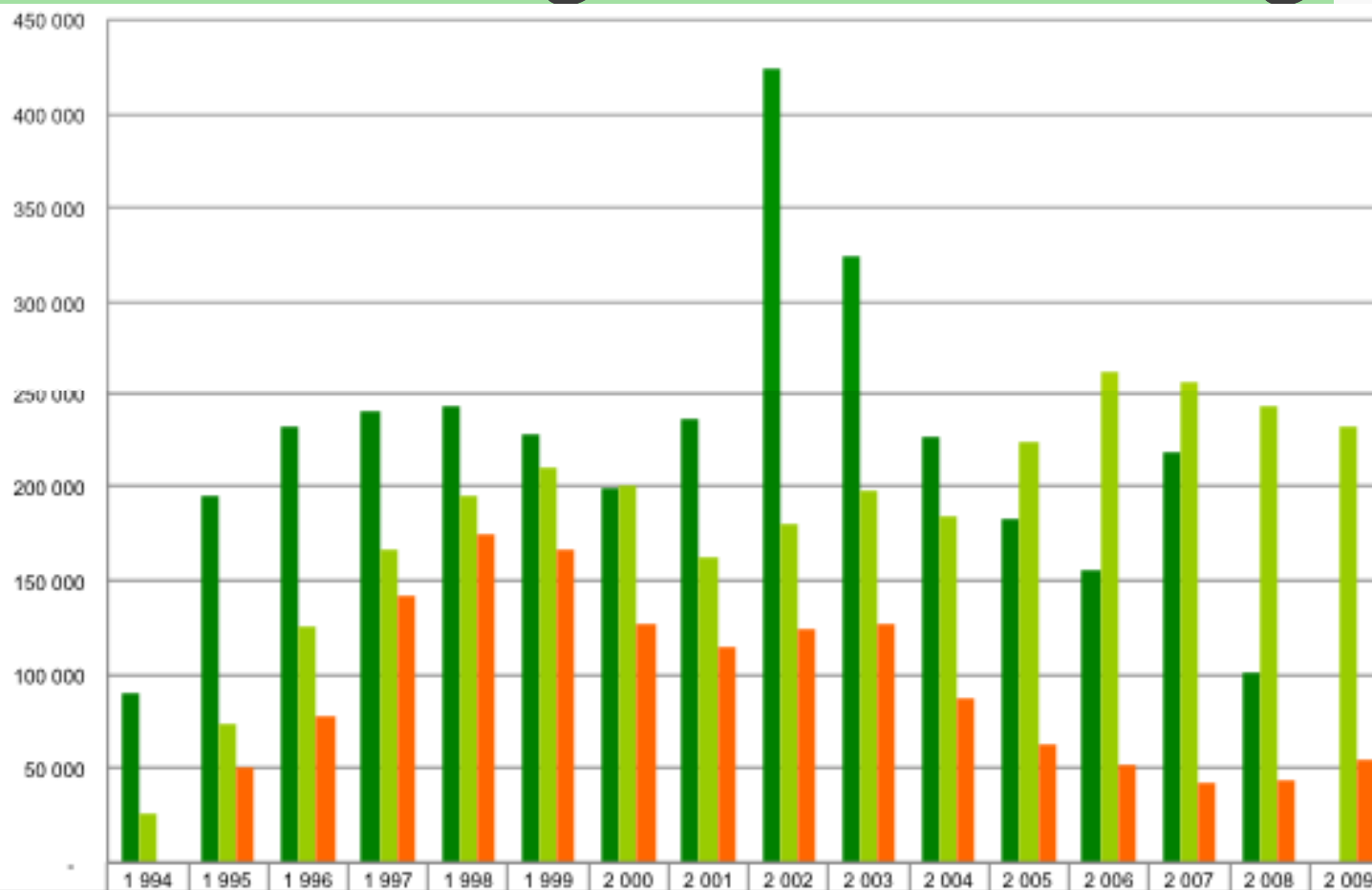
a. Insufficient Delivery

- Impressive progress since 1994 unfortunately no longer sufficient
 - Nearly 3 million fully subsidised houses since 1994 (average of 167,000 houses per year);
 - Rising backlog - More than 2 million households are presumed homeless in South Africa
 - Exploding housing waiting lists
- Needs of lower income households not being met
 - Historical issues of size of subsidy and availability of credit
 - Distortionary effects of subsidy: gap market
- Poor data and understanding of housing demand
 - While stakeholders agreed that the demand for adequate housing remains high, it is difficult to ascertain accurately the extent of this because of poor data on past delivery, trends, needs and effective demand
 - Good data is needed and can be used to improve understanding of the current situation and to inform housing policy

Rising Backlog



Outputs (1994 – 2009) below 300 000 target and declining

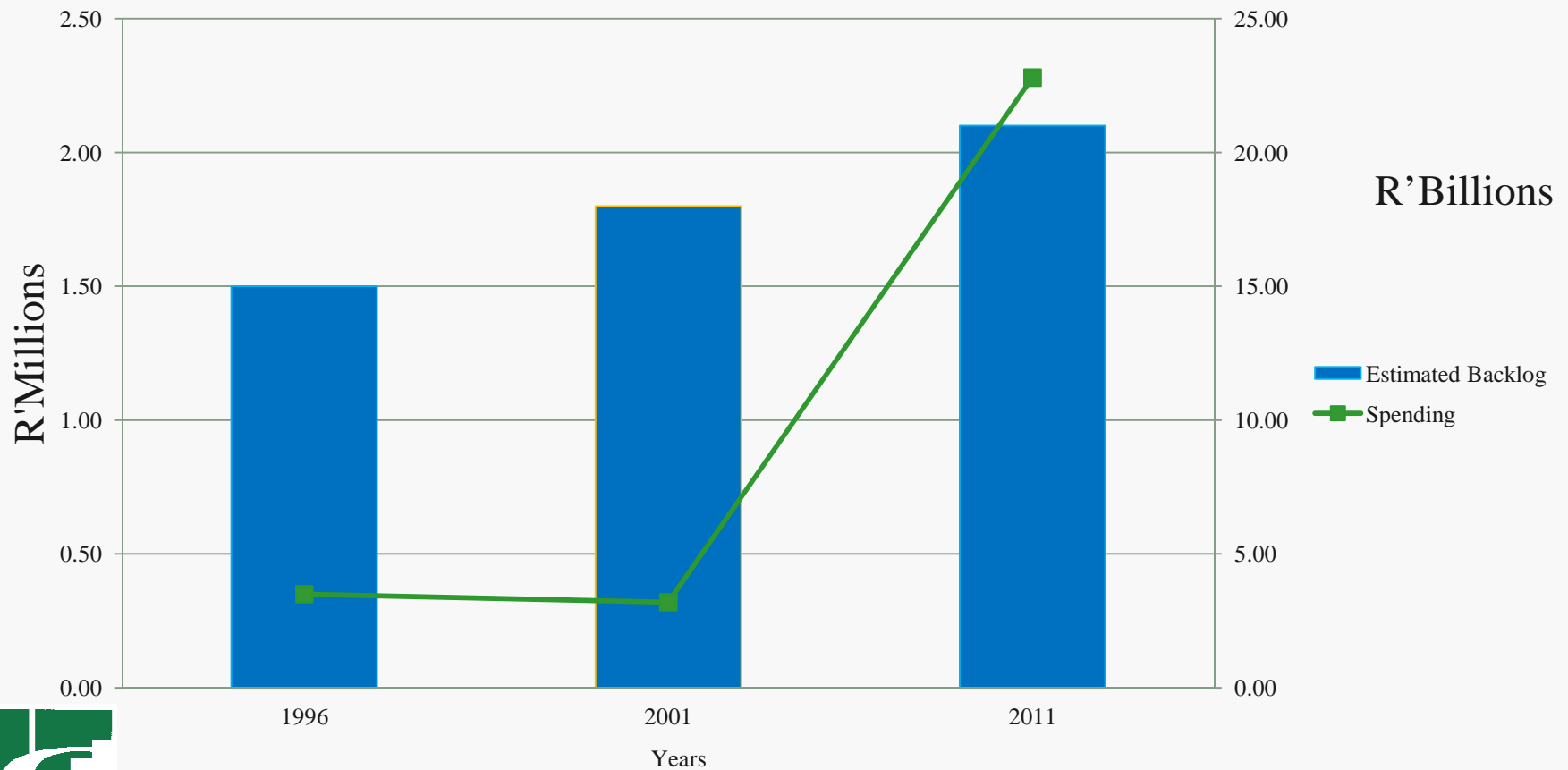


■ Number of subsidies approved	90 107	195 232	232 025	240 079	242 808	228 467	198 838	236 470	424 843	324 882	225 885	182 664	155 012	217 848	100 826	
■ No of houses completed/under construction	26 502	73 321	126 147	166 218	194 705	210 821	200 058	162 226	179 465	197 604	184 613	223 145	263 865	257 798	243 260	231 543
■ Total number of subsidy properties registered		51 106	77 413	141 858	174 256	167 056	127 167	114 395	123 917	127 472	87 195	62 644	51 950	42 302	43 891	54 265

b. Sustainability

- The budget allocated has increased significantly but has not resulted in increased delivery
- As costs increase over time, even higher levels of subsidies are required to deliver on promises, which makes the current housing finance policy unsustainable
- To eliminate housing backlog at a cost of R140 000 per unit, about R300 billion is required - a sum far beyond the fiscal capacity of the state
- Assuming a delivery rate of 250 000 houses per year, the annual budgetary implication is R35 billion

Rising Backlogs vs. Spending

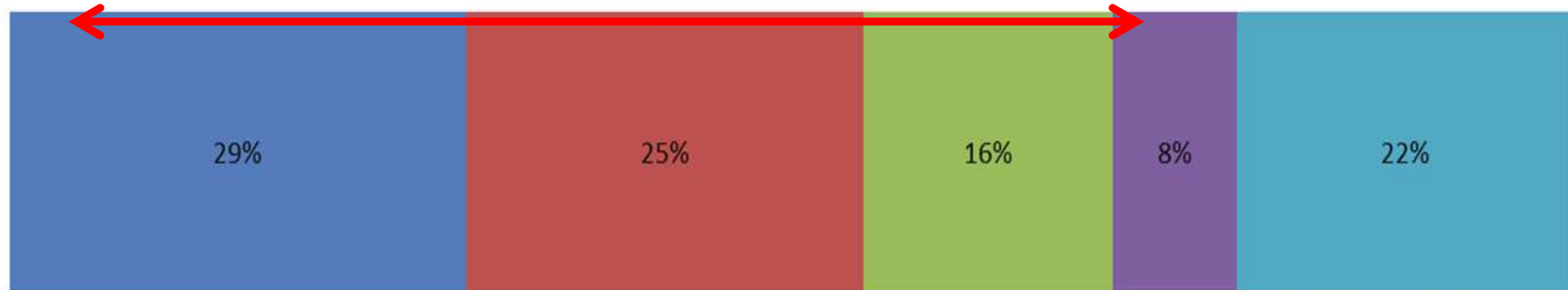


c. Affordability

- Average price of house is over R500 000 (*Affordable Land and Housing Data Centre*)
- Household earning about R10,000 per month could afford the cheapest house costing about R250,000
 - However, delivery in this segment of the market is far below the estimated demand
 - According to the Affordable Land and Housing Data Centre, in 2010 only 6,252 new units priced between R250,000 and R500,000 were registered on the Deeds Registry
 - Shortfall of 5 to 6 million properties under R100 000 (Lightstone, 2011)
 - Banks are willing to offer unsecured loans to households earning above R2000 per month, but offer no commercial incremental housing product
 - On average housing delivery takes 3 years from land assembly to final handover. Long bureaucratic delays increase cost of houses which developers pass on to end users, making prices even more unaffordable.

Proportion of Households Per Income Category

Households by income



- Household income less than R1500 per month
- Household income between R 1500 and R3500 per month
- Household income between R3500 and R7500 per month
- Household income between R7500 and R12500 per month
- Household income greater than R12500 per month

d. Informal Settlements Growth are an Emergency

Growth in Informal Settlements



- Nationally 10 shack fires each day, over 200 deaths p.a.
- 7% HIV annual incidence rate - 1.8% in urban formal areas
- Diarrhoea-related infant mortality up to 10 times higher than urban formal areas
- Official estimates over 40% unemployment compared to 26% national average

Service delivery protests average two per week

... and Informality May Be Part of the Solution

- Accepting informality as a reality and as a point of entry into the housing market
 - Stakeholders suggested that the 60% at the bottom of the market could access decent housing only through combination of informal self-build and government financing assistance
 - Could have a real impact on reducing backlogs
- Shift from a focus on ownership to all forms of housing supply is required
 - Instead of a narrow focus on ownership, there is need to consider other forms of tenure (e.g. rental housing) and incentivising them where possible

e. Barriers in the Delivery Chain

- Supply and access to well-located land and bulk infrastructure as well as housing delivery chain inefficiencies
 - Stakeholders agreed with the FFC that main challenges for affordable housing supply include access to well-located land and bulk infrastructure
 - Inefficiencies in the housing delivery chain
 - Poor targeting of the subsidy
 - More than 51% of subsidy houses not registered at deeds office
 - Although up to 70,000 hectares of state-owned land have been identified for housing developments, none have been made available for this purpose
- Intergovernmental coordination and leadership
 - Perception of a “one size fits all” approach
 - insufficient authority and responsibility at municipal level (limited accreditation?)
 - Weak inter-sector planning and lack of long-term spatial planning
 - Non-complementary zoning and land use management practices



2.3 Research Gaps

Research Gaps Identified

- Building a single, inclusionary housing market
 - Formal and informal markets are operating, although under severe stress and with exclusion of the poorest
 - State financed houses will always remain only one component of the overall market
- Clarifying the role of state in housing provision including options for public finance
 - Financier: public good vs. private good dimension
 - Demand vs. supply side
 - Non-fiscal instruments
 - Infrastructure financing
 - Land use planning

Research Gaps Identified

- Rethinking housing entitlements
 - Households should be actively engaged in determining and meeting their housing needs
 - In Latin America and Asia, informal settlements evolve into formal settlements; in SA they remain long term as potential beneficiaries wait for the government to provide
- Address the needs of people living in informal settlements
 - Informality reflects both state and market failure, but must be addressed directly
 - Informality is not a problem, but an opportunity to redesign our cities and social relations



Building active property market in the townships

Research Gaps Identified

- Understanding demand for housing: what do households want?
 - Housing life cycle
 - Credible data on current and projected housing needs
 - Affordability and unlocking effective demand
- Unlocking supply
 - Land acquisition and production
 - Housing finance (crowding in private sector)
 - Regulatory constraints:
 - Quantifying the cost of delays and how such delays could be minimised
 - Land use management regulations (zoning, development control)
 - Role of public transport

Research Gaps Identified

- Sustainability of the current delivery model
 - Fiscal gap and implications
 - Impacts of new instruments (new guarantees)
- Institutional arrangements
 - Unexplored partnerships
 - Intergovernmental arrangements and relationships
- Leveraging household and private finance
 - Crowding in private sector
 - Household savings and investments



Thank You!