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GORDON INSTITUTE  
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# **“Social housing in South Africa: are public private partnerships (PPP) a solution?”**

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## **ABSTRACT**

South Africa faces a shortfall in its provision of housing for low income households. This study explores the potential to use public private partnerships (PPP) to address these supply problems. A review of the housing market and an examination of the opportunities and challenges presented by PPP are presented, including a review of the international experience in the provision of social housing. Interviews with key stakeholders are undertaken to evaluate the appropriateness of PPP in the South African social housing sector. PPP are believed to have the potential increase the supply of social housing, provided there is continuing support from the state. However, none of the key stakeholders were keen to use the “traditional” PPP process, suggesting a need for innovative partnership models more appropriate for the sector.

### **Keywords**

Public private partnerships, private finance, social housing, South Africa.

## DECLARATION

I declare that this research project is my own work. It is submitted in partial fulfilment of the degree of Master in Business Administration at the Gordon Institute of Business Science, University of Pretoria. It has not been submitted before for any degree or examination in any other University. I further declare that I have obtained the necessary authorisation and consent to carry out this research.

.....

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Yandisa Sobuza

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# 1 CHAPTER 1: INTRODUCTION TO THE RESEARCH PROBLEM

## 1.1 Description of the problem and background

Excessive levels of urbanisation in relation to economic growth have resulted in high levels of urban poverty and rapid expansion of unplanned urban settlements and slums, which are characterized by a lack of basic infrastructure and services, overcrowding and substandard housing conditions (UNCHS, 2008). This rapid growth in urban populations is overwhelming efforts to provide adequate housing, thereby, widening the gap between the demand and supply of housing, especially for low income sectors (Sivam, Evans, King, and Young, 2001). For three decades now, governments all around the world have tried to address the problem of providing adequate and affordable housing (Ong & Lenard, 2002) with an enhanced recognition of the need for new approaches to deliver more affordable housing.

South Africa is one of many countries facing housing challenges. The national department of human settlements (NDHS) had put forward a plan and a target to house all informal settlements; fast track the provision of formal housing and make rental stock available to the urban population within city environments by 2014 (NDHS, 2004). Despite impressive efforts being made, housing still

remains a major challenge in South Africa, as millions of people are still inadequately housed.

Furthermore, many stakeholders, including the government, are concerned about the poor quality of housing stock delivered in South Africa (Sigodi Marah Martin & Matthew Nell & Associates, Joint Venture, 2002).

As a result, there has been recognition of a need to promote alternative options to address the various housing needs of the South African population, including the promotion of social housing to provide integrated and sustainable human settlements. In South Africa, the term "social housing" is often used to refer to "a rental housing option for low-to-medium income persons that is provided by housing institutions and that excludes immediate individual ownership" (NDHS, 2005).

According to Sigodi *et al.* (2002), social housing has developed very slowly, and delivery has been limited. Delivery to date in the sector has resulted in the order of roughly 30,000 social housing units being under management country wide over a 10 year period (NDHS, 2005), which is low in the context of increasing demand and government's target of delivering 50 000 within 5 years.

The South African government's Social Housing Policy (NDHS, 2005) proposed Public private partnerships (PPP) as a second component of government's three-pronged strategy for gearing to scale in this sector. PPP are viewed as a vehicle for "fast-tracked" delivery of social housing. PPP have also been

suggested by researchers as a vehicle to increase the supply of social housing (UNCHS, 2007; Anderson & Thompson, 1999; Moskalyk, 2008).

Public private partnership refers to a contractual agreement between a government agency and a private sector entity that allows for greater private sector participation in the delivery of public infrastructure projects (Deloitte Research, 2006). Amidst increasingly constrained public budgets, housing shortages, and inadequate supply of housing, globally, PPP have emerged as one of the major approaches to supplement traditional public sector funding models for delivering public infrastructure and related services by using private funding (Broadbent & Laughlin, 2003; Edwards & Shaoul, 2003). Compared to traditional procurement models, the private sector assumes a greater role in the planning, financing, design, construction, operation, and maintenance of infrastructure or public facilities.

Whilst the development of PPP has predominantly concentrated on a few sectors (e.g. transport), there has been a growing use of PPP in managing affordable housing, both in the construction of new affordable housing and in the management of existing developments (Li & Akintoye, 2003), as countries move up the PPP maturity curve. Researchers suggest that PPP have entered into the mainstream of urban development practice and that many variations on this are evolving to respond to different conditions and needs (Payne, 2003).

Consequently, PPP have been researched considerably in the “traditional” sectors. Although the opportunities and risks of PPP have been extensively debated in the broader literature, the role of such partnerships in social housing has received comparatively little attention (Susilawati & Armitage, 2004). There are aspects of PPP that are not clear to all participants and there are contrasting views on the suitability of PPP in the “non traditional” social infrastructure sectors including social housing delivery (Susilawati & Armitage, 2004).

Internationally, there have been a few studies assessing the viability of PPP in social housing (Susilawati & Armitage (2004) in Queensland, Australia; Moskalyk (2008) in Canada) and these studies had different findings, reflecting the differences in the housing policies, political, socio-economic, cultural and institutional contexts in the those countries. It has also been argued that the PPP are not the same across countries in the context of their formation and operation (Xie, 2002; Keating, 1998).

In the South African context, no empirically based research that focused on South African instances of PPP in social housing was found. To fill this knowledge gap, this study is an opportunity to generate research that assesses social housing in the South African context.

With the recognition of the potential contribution of PPP in the South African social housing policy, it is the opportune time to ask whether this option is being

utilised to the full extent possible in the South African housing sector and what, if any, changes are needed to unlock the potential which lies within?

The research was therefore motivated by:

- The need to establish innovative mutual delivery models for social housing delivery in the wake of current supply shortfalls and inadequate delivery by current models
- The fact that PPP, as a method of delivery for social housing has not been empirically tested in South Africa.

It is hoped that the outcome of this research project will be useful to decision makers in both the public and private sectors in setting policy focus, and in the development of appropriate delivery models to meet South Africa's housing needs.

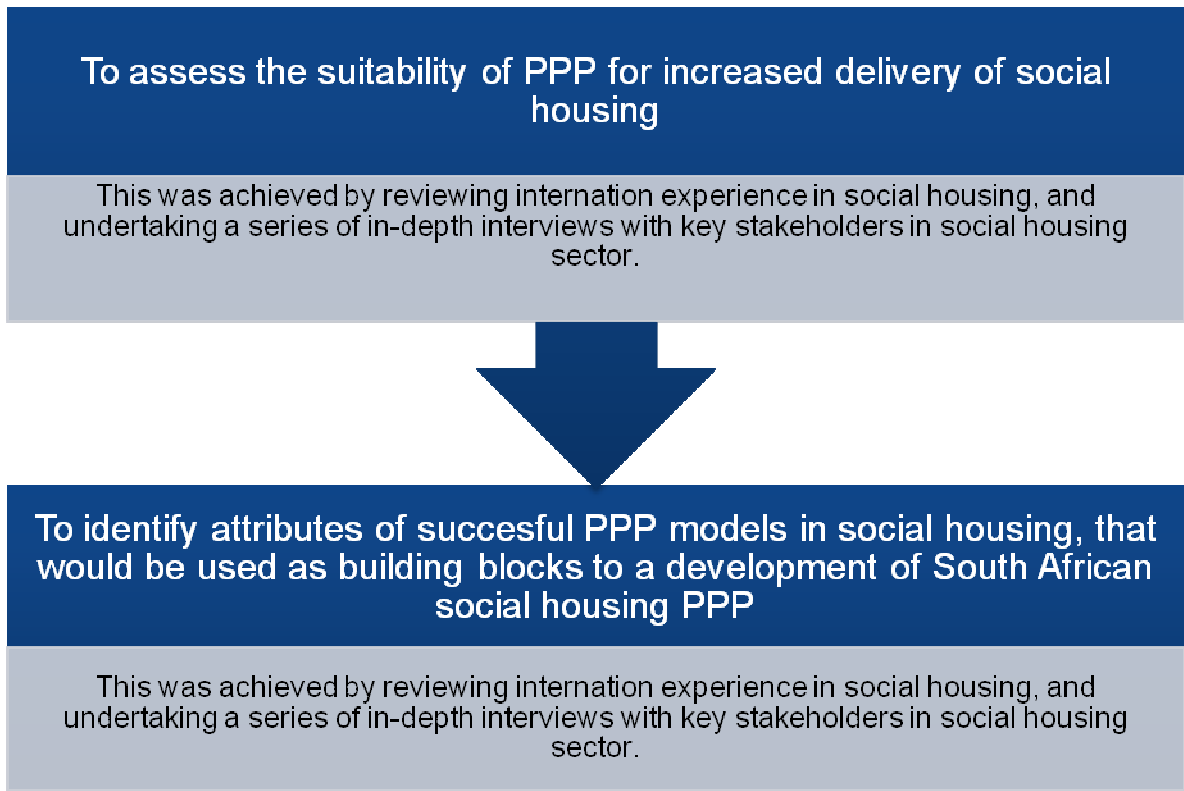
## 1.2 Research Objectives

The research aimed to investigate the role that PPP can play in facilitating large scale delivery of quality social housing in South Africa. The main objectives for the study as illustrated in Figure 1 below were therefore:

- To assess stakeholder's perceptions on whether PPP are an appropriate and effective mechanism for the delivery of increased quality and sustainable social housing in South Africa

- To identify key attributes of successful PPP models from international best practise, which could be used as a building block for the development of South African social housing partnerships.

**Figure 1.1: Research Objectives**



### 1.3 Research Scope

The scope of this research covered the factors that facilitate the adoption of the PPP framework and barriers that hinder implementation, the opportunities, and risks presented by PPP and their suitability for social housing.

While PPP have been extensively researched globally, the literature has mainly focused on the implementation of PPP in economic infrastructure and there has been insufficient attention given to the social infrastructure projects (Susilawati, & Armitage, 2004). In addition, housing policies, national political and institutional frameworks, and PPP definition vary in different countries. Hence the need for the study in a South African context. The scope of this research was, therefore, limited to the South African social housing sector market.

## **1.4 Summary**

This chapter has provided the case for the examination of PPP in the South African Social Housing context. The next section, chapter 2 provides a contextual background highlighting the main drivers for PPP adoption in social housing. Chapter 3 presents a critical review of the literature on PPP and Chapter 4 the questions to be answered by this research. The results of the empirical research are discussed and analysed in the remaining chapters, including recommendations for the South African context.



## **2 CHAPTER 2: CONTEXTUAL BACKGROUND: THE SOUTH AFRICAN HOUSING MARKET**

### **2.1 Introduction**

The South African housing market has many unique features that make a direct replication of other countries' housing policies, without an understanding of the historical context, ineffective. This section presents the contextual background in the South African housing market that has led to the search for alternative delivery options. The section begins with a review of the historical policy background, followed by an examination of the rental social housing market, the current situation and the challenges to the growth of the social housing sector, closing by highlighting the main drivers of PPP adoption in the sector. Given these challenges, a question is asked, why PPP?

### **2.2 Historical background**

South Africa is characterised by a growing population that is becoming more and more urban. Many South Africans currently live in inadequate shelter, mainly in overcrowded informal settlements with poor access to basic services such as water and sanitation. Most importantly, the housing crisis is an important dimension of the overall poverty problem in South Africa.

The national housing policy framework and the housing challenges can be traced back to the past political systems, which have left a legacy of backlogs in housing delivery, unequal and racially stratified settlement patterns. This legacy has caused the confinement of the majority of non-white South Africans, to certain areas, usually located on the periphery of urban centres, excluded from service delivery, infrastructure, and economic opportunities.

### **2.2.1 The policy focus in 1994**

The South African Reconstruction and Development Programme (RDP) housing delivery began after the 1994 elections with a narrowly focussed commitment to increasing the quantity of housing stock available to the poor as quickly as administratively possible (Barry, Dewar, Whittal & Muzondo, 2007). Over the past decade, low income housing has been strongly focussed on delivery of subsidised housing units; (i.e. the emphasis was on the construction and transfer of units to individual owners, where long-term maintenance was the responsibility of the owners).

This form of tenure has provided houses to millions of South Africans in the low income categories. In his address, on the occasion of the human settlements budget vote, (National Assembly, Cape Town on the 21 April 2010), the national department of human settlements' Minister, Mr. Tokyo Sexwale, reported that..."*since 1994, more than 2.3 million housing units have been made available for nearly 11 million people. Despite the impressive delivery of*

*houses, the housing backlog has increased from 1.5-million in 1994 and now stands at approximately 2.1 million. That means approximately 12 million South Africans are still in need of better shelter.”*

Further concerns in respect of the current housing crises, relate to the poor quality of stock provided and the continuation of creation of undesirable urban forms.

In light of these challenges, a new policy was introduced in 2004 that was aimed at addressing the rising backlog and improving housing delivery.

### **2.2.2 The policy shift in 2004: breaking new ground**

In 2004, there was a major shift in housing policy with the introduction of the breaking new ground (BNG) plan, marking a turnaround in housing delivery. The strategy focussed policy attention on the development of sustainable human settlements, as opposed to the delivery of subsidised housing units. BNG re-evaluated housing delivery and recommended bold changes to the traditional ways in which housing had been delivered. “The new human settlements plan reinforces the vision of the department of human settlements, to promote the achievement of a non-racial, integrated society through the development of sustainable settlements and quality housing.” (NDHS, 2004).

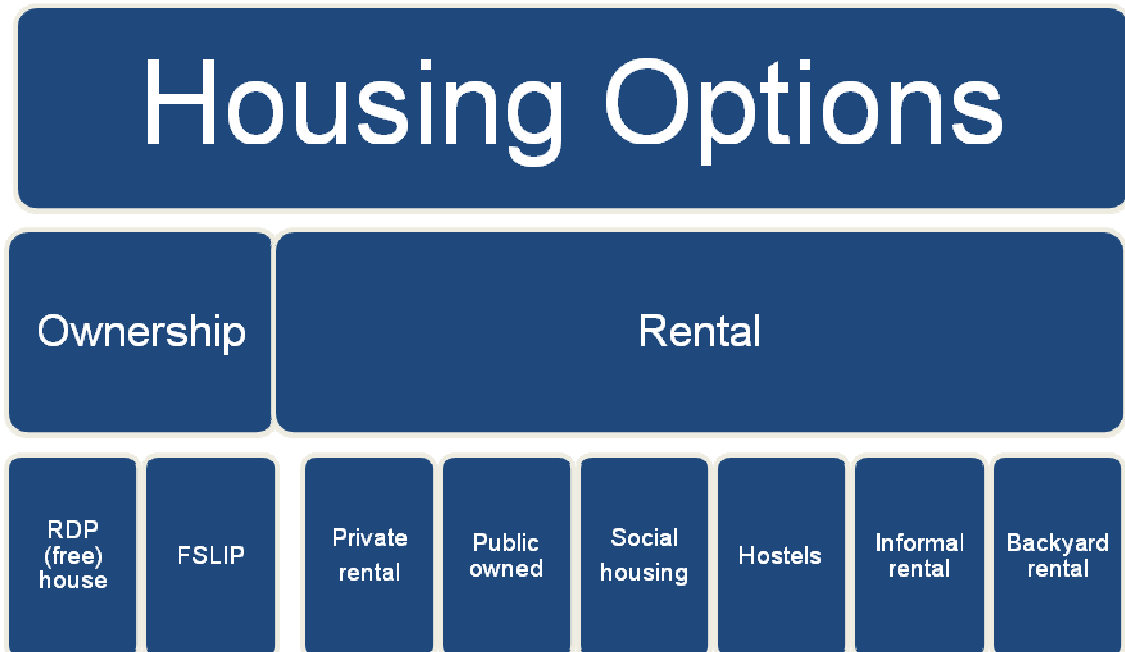
The sustainable human settlements discourse, as articulated in BNG, is couched within the emerging international language for addressing global

housing, as encapsulated in the goals, principles and commitments set out in the Habitat Agenda and Global Plan of Action, endorsed by world governments for urban sustainability (NDHS, 2004).

The BNG plan introduced new options for delivery and a range of delivery options, with an emphasis on rental housing as a form of tenure, recognising it as a significant contributor to meeting the housing challenges in South Africa. This was in line with the trend in both developed and developing countries, where the potential of the rental sector to contribute towards urban renewal and poverty alleviation is increasingly recognised. International best practice shows that a layering of different delivery mechanisms is required to fast track affordable housing delivery, and that a balanced approach which uses both rental and ownership tenures, where appropriate, to meet the specific needs of low income households is more appropriate than narrowly focusing on one mode. Rental and ownership housing together create a healthy and vibrant housing sector and meets the range of choices that meets the economic needs and lifestyle choices of consumers (Sigodi *et al.*, 2002).

Figure 2 below illustrates the different housing options promoted by the South African department of human settlements, demonstrating a balance between ownership and rental, a departure from quantity of housing and the existing subsidy led low income housing delivery to an integrated approach embracing different tenures and promoting the health of human settlements.

**Figure 2.1: Housing tenure options**



## 2.3 Social housing

### 2.3.1 Defining social housing

Between 1995 and 2000, the concept of social housing was introduced, and a social housing policy (SHP) was introduced. Since then, the sector has undergone changes. A revised social housing policy was introduced in 2008. Pursuant to the SHP, the social housing regulatory authority (SHRA) was established by the NDHS (NDHS).

In South Africa, social housing is defined as “a rental or co-operative housing option for low income persons at a level of scale and a built form which requires

institutionalized management and which is provided by accredited social housing institutions or in accredited social housing projects in designated restructuring zones”. (NDHS, 2005). Social housing primarily covers the rental tenure option and excludes immediate individual ownership by the residents.

### 2.3.2 The targeted market for social housing

The majority of the low to middle income households in South Africa have challenges accessing the limited number of well located, affordable rental opportunities provided by the formal market. Social housing involves the creation of affordable housing stock primarily for low to middle income households, broadly defined as household income in a range of R1500-R7500 per month (NDHS, 2005), as classified as per the Table 2.1. Social housing is intended to be an important contributor to the housing options for the low to middle income households and to the national housing sector.

**Table 2.1: Income classification**

Classification	Income	Subsidy
Middle income	R3500 – R7500	Rental
Low income	R1500 – R3500	Rental and partly subsidised ownership
Poor	<R1500	Fully subsidised ownership
Destitute	0	Fully subsidised ownership

### 2.3.3 The relationship of social housing to the broader housing market

The BNG housing strategy (2004), explicitly carved an important role for social housing in the broader housing framework. “.Social housing has shown that it is able to significantly contribute to *urban regeneration* and to *urban efficiency*. It can meet objectives of *good location, integration, and viability*. ... Social housing has been shown to promote the effective and efficient management of rental and/or collective forms of accommodation (with emphasis on long term management and maintenance). This contributes to *social integration, social stabilisation, and crime reduction*.”

The main justification of social housing policy is to promote restructuring and social integration, balanced with the intention of achieving deep, down market reach on the one hand, and balanced communities in socioeconomic terms. Social housing excludes the destitute (see Table 2.1) and is targeted at earners with the ability to pay rental. The poor and destitute housing needs are accommodated by other options that have been created within the housing subsidy scheme (HSS) (see Table 2.1). The sector offers choice, mobility and an opportunity for those households that do not qualify for a fully subsidised ownership subsidy but are also not in a position to qualify for a mortgage (NDHS, 2005).

Social housing is, therefore, one means of catering for the variety of housing needs of the different income groups. While the proportion of rental

accommodation to ownership varies in different areas, there is a consensus that those housing sectors that are functioning well have a good balance between ownership and rental (NDHS, 2005).

### **2.3.4 Social housing delivery agents**

#### **2.3.4.1 *Social housing institutions (SHI)***

SHI are envisaged in the social housing policy to be the primary delivery vehicle of social housing (either as SHI or via PPP). They are categorised as not-for-profit organisations. SHI were developed in South Africa since 1997 with the introduction of the institutional subsidy mechanism. An SHI accreditation mechanism was established to regulate and provide compliance criteria for SHI to ensure that their operational viability is safeguarded and will provide a measure of comfort to any financial institution from which the SHI may wish to borrow for project development.

According to the department of human settlements, there are about 60 registered SHI. These institutions have developed social housing stock using the institutional subsidy together with loan funding from the National Housing Finance Corporation (NHFC) and have relied on donor funding and local authority grant funding to cover institutional set-up and operational costs. This has resulted in an unsustainable situation where the majority of the SHI have depended on donor funding (NDHS, 2005).



The social housing policy also highlights that SHI could also include municipal entities defined in terms of the Municipal Systems Act no. 32 of 2000.

#### **2.3.4.2 *The Private sector***

In addition to SHI, private for profit entities (developers and investors) are able to develop and/or manage accredited social housing projects for low income residents in restructuring areas by assessing the new restructuring capital grant. The restructuring capital grant is only applicable for the rental tenure, in projects that have been approved by the designated regulatory body. An accredited project is a project in which government makes a subsidy contribution in order to make rental units that are provided by a private sector party more affordable to those eligible for social housing.

The social housing grant is held in a ring-fenced property holding company, and at the end of the project's lifetime, the public sector retains the stock. This does not require participation of a SHI.

The notion of accredited projects allows for the participation of private sector developers and rental management agencies in social housing provision in order to bolster capacity to achieve scale delivery.

#### **2.3.4.3 *PPP***

Another delivery mechanism identified in the SHP is the use of public private partnerships (PPP), for big impact projects in designated restructuring areas.

The partnerships would include private for profit entities and the SHI that would be actively involved from the start of the conceptualization and development of a project. The private sector is seen to play a key role in the conceptualization, construction, and management of PPP projects.

The build-operate-transfer (BOT) model introduced by the SHP requires private sector companies to build and operate social housing projects for a concession period of not less than 15 years. The private firm will then be free to make market related decisions and trade with the housing stock now at their disposal. They would be in a favourable position to realize a substantial return. (Trusler & Cloete, 2009)

#### **2.3.4.4 Government funding support for social housing**

There are two subsidy mechanisms to support social housing:

- *The institutional subsidy mechanism:* was introduced to cover the development costs of units for households earning less than R3 500 per month paid to SHI that develop social housing stock
- *The restructuring capital grant:* was made available by the revised SHP for social housing projects in certain geographic restructuring zones. The private sector can access this grant for registered social housing projects. Those projects have to qualify in terms of a number of criteria, including the financial viability of the project, its state of readiness for delivery, and its

targeted rentals. At least 30% of the units in the project must have rentals that are targeted at the 'Primary Target Market', (30% of the average household income of between R1 500 and R3 500 per month).

#### **2.3.4.5 Demand for rental housing**

To understand the housing challenges in South Africa, it is important to look at income distribution of the South African population. Table 2.2 (adapted from Rust, 2006) below, illustrates housing sub-markets, the proportion of South African households each one represents and outlines general levels of housing affordability.

**Table 2.2: Demand of rental housing**

Classification		Income R/month	% of South African Households	Subsidy Eligibility	Rental Affordability 25% of income (R/m)
Max	Very High	>8,001	10%	No	
Min		7,500			<i>R 1,875.00</i>
Max	High	7,499	4%	Rental	<i>R 1,874.75</i>
Min		5,500			<i>R 1,375.00</i>
Max	Mid-High	5,499	3%	Rental	<i>R 1,374.75</i>
Min		4,500			<i>R 1,125.00</i>
Max	Middle	4,499	4%	Rental	<i>R 1,124.75</i>
Min		3,500			<i>R 875.00</i>
Max	Moderate	3,499	6%	Rental/ Ownership	<i>R 874.75</i>
Min		2,500			<i>R 625.00</i>
Max	Low Income	2,499	10%	Rental/ Ownership	<i>R 624.75</i>
Min		1,500			<i>R 375.00</i>
Max	Very Low income	1,499	25%	Ownership	<i>R 374.75</i>
Min		1			
Max	No wage income	500	38%	Ownership	<i>0</i>
Min		0			

*Source: Adapted from Rust (2006)*

The table above illustrate the following important features of the South African housing market, household income distribution, and rental affordability:-

- Housing affordability is very low. A high proportion of all households in South Africa are in the lower income categories, where the majority of (79%) has a household income of less than R3500.
- As much as 63% of the population is dependent on the state subsidy for meeting their housing circumstances (Rust, 2006) and cannot afford rent. Rental affordability, assumed to be 25% of the income, except in

Gauteng where the figure is 30% of income per month, is limited to rents of about R1800.00 per month.

- The social housing market (with household incomes of between R1500 to R3500 per month), makes up 27% of the South African population.

According to Rust, (2006) in 2005, Shisaka development management services (SDMS) estimated that 3,5 million households, or 27% of the population, live in rental housing. The potential social housing sector is anticipating strong growth, estimating at about 5% per annum (Rust, 2006).

#### **2.3.4.6 Social housing supply**

Despite the establishment of focussed institutions to encourage this form of housing delivery, social housing has developed very slowly, and delivery has been very limited. To date approximately 60 social housing institutions (SHI) have been formed, delivering approximately 30,332 units throughout the country (NDHS, 2005), at a delivery rate of 25,000 social housing units over 10 years. The Brickfields PPP project, which was funded by a combination of institutional subsidies, equity, grants, and debt funding has delivered 700 social housing units.

In comparison, the private sector formal rental market, which has not accessed the government subsidies to date, through the property owners and managers

association (POMA), an association of private sector landlords in the Johannesburg inner city, owns amongst its members more than 100 000 units.

However, there is no available information on the tenant income profile catered for by the private profit property owners to accurately determine the percentage of the units for the affordable market. According to Rust (2006), these formal providers of affordable rental housing opted, in many cases, to deliver housing without accessing the subsidies.

When measured against international norms, the social housing sector in South Africa is underdeveloped (NDHS, 2005). Noting the disappointing record of accomplishment to date of SHI, the department of human settlements suggests that the sector is hampered by serious constraints. The next section reviews those constraints.

#### **2.3.4.7 Challenges in social housing delivery**

According to the department of human settlements, a diagnostic review by the support programme for social housing (SPSH) found that only a limited number of SHI are performing and delivering housing units, and many of them are in financial distress and/or suffering from governance deficiencies.

The housing institutions are mostly characterised by small organisations with limited resources.

The reviews of the sector highlighted the following challenges in this sector:

#### 2.3.4.7.1 Financial constraints

- The overall funding framework and the current institutional subsidy is not tailored to the production of viable medium to higher density housing products and projects, and has no proper provisions for the operating and management costs of the housing stock
- Financial pressures are immense and the parameters of the current subsidy approach are too tight to allow the provision of social housing too far down-market. In most cases SHI display serious financial distress
- Access to finance is a problem. At current subsidy levels, in respect of new housing construction and conversions, social housing institutions are failing to achieve returns on capital, sufficient to match inflation. The sector has been moving out of the low income market into the middle income markets due to the financial pressures
- To be sustainable, social housing institutions require substantial funding in the form of grants or soft loans in the early years
- Social housing is highly dependent on efficient government systems for allocating the institutional subsidy.

#### 2.3.4.7.2 Capacity constraints

- Social housing is a relatively new niche and not fully understood and the capacity of agents in social housing is limited. Although experience has grown in this sector, genuine SHI experience is limited
- Capacity constraints exist in all spheres of government and have been experienced most acutely at local government level. The ability of local government to facilitate the establishment of sustainable housing environments is threatened by a lack of capacity to effectively package and align departmental funding streams, employ innovative planning principles, acquire affordable land and sustain a dedicated group of officials
- A lack of suitable governance and management capacity has been evident within some of the SHI ,
- Scale is hard to achieve in the sector within the current context, given that the capacity and experience base is limited and needs to be consolidated and properly reinforced if scale is an objective
- Capacity building initiatives for the sector have largely centred on education and training initiatives and the pre-establishment phase of the SHI. This has resulted in a focus on the establishment of SHI with limited emphasis on the project packaging, project implementation and project operations skills needed to run viable institutions.



#### 2.3.4.7.3 **Unsupportive policy environment**

- The department of human settlement also conceded that the policy and funding environment has been very unsupportive in this sector. It is also apparent that the current distress that the sector finds itself in is, at least in part, due to the absence of an effective monitoring system with a capacity to intervene early to address problems (NDHS, 2005)

#### 2.3.4.7.4 **The cost and access to land**

- The identification, acquisition, assembly, and release of state owned and private land in terms of the revised procurement framework has proved to be a slow and complex process. The housing development agency (HAD) has been recently established to address this problem and unlock government land for housing developments. However, it has yet to make an impact.

### 2.3.5 **Is the PPP a solution?**

Given the above constraints, there is a growing recognition for the need for alternative sources of finance and delivery mechanisms if the sector is to achieve its targets and contribute to addressing the housing needs of the low income households in South Africa. PPP are proposed as one such vehicle. The international literature indicates that in most European countries finance, or the lack thereof, was the key impetus behind the drive for increasing private sector involvement in the social housing sector. As public funding has been cut

back, social landlords have been forced to look for other sources of finance for regeneration projects (Scanlon and Whitehead, 2007).

Furthermore, a PPP is attractive (as summarized in the table below) because:-

- It involves efficient pooling of resources, by making optimum use of private sector financial, management, skills and expertise;
- Risks are managed and shared better where risks are allocated to the party best able to manage;

The table below further illustrates the suggested drivers and benefits for using PPP that would boost the growth prospects of the sector:-

**Table 2.3: Why PPP?**

<b>Problem identified with SHI</b>	<b>PPP solution?</b>	<b>PPP Benefit</b>
<b>Financial constraints</b>		
The funding gap (Capex)	Yes	Access to debt funding
The funding gap (Opex)	Yes	Access to debt funding
High operating expenses		Efficiency gains resulting in cost savings
<b>Capacity Constraints</b>		
A lack of management capacity amongst most SHI	Yes	Can increase the resources and expertise available for social housing projects

## 2.4 Summary

Given these potential benefits, it is worth exploring whether PPP can live up to the promise they hold.

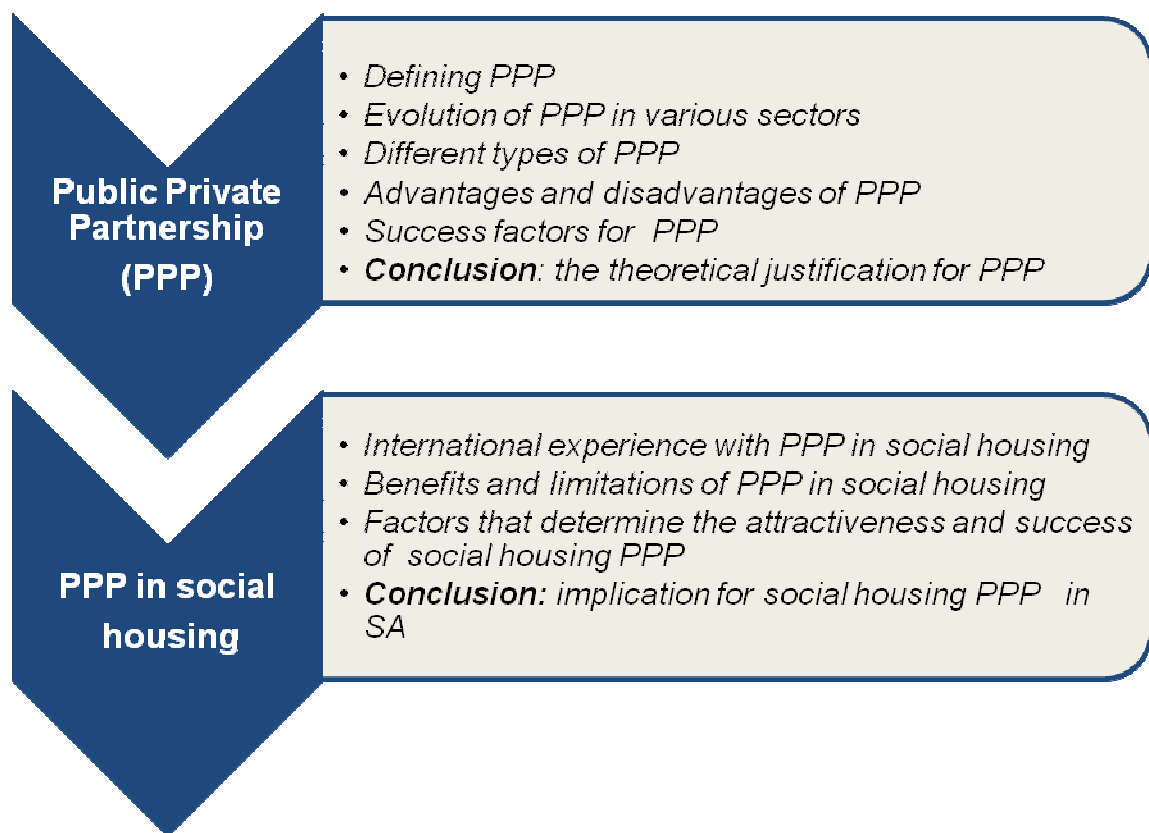
This section reviewed the current housing situation in South Africa, highlighting the factors that have inhibited the supply of housing leading to an alternate search for delivery mechanisms in social housing delivery. The main factors identified as inhibiting the growth of the sector were the capacity constraints and financial pressures constraints evident in the social housing market. The next section presents a review of the current literature regarding the opportunities and challenges presented by PPP, highlighting the insights on the potential of its application in social housing.

## 3 CHAPTER 3: LITERATURE REVIEW

### 3.1 Introduction

The literature review is divided into two main sections as illustrated in Figure 3

Figure 3.1: Structure of Literature review



## **3.2 Public private partnerships**

### **3.2.1 Introduction**

The first section is a review of the literature in PPP, examining the PPP approach and the rationale underpinning them and the opportunities and challenges presented by PPP in general to provide insights into how this approach can be used in social housing.

### **3.2.2 The elusive definition of public private partnerships**

The literature around public private partnerships (PPP) indicates that PPP are notoriously difficult to define (Evans & Bowman, 2005; Hodge, 2005; Jefferies & McGeorge, 2008). Bettignies & Ross, (2004) point to the fact that PPP have been defined differently by several academics, public agencies and international organisations, with the result that a universal definition to which all would agree are elusive.

In Canada, the Canadian council for public private partnerships (2003) defines PPP as "a cooperative venture between the public and private sectors, built on the expertise of each partner, that best meets clearly defined public needs through the appropriate allocation of resources, risks and rewards."

In the United Kingdom (UK), HM Treasury defines PPP as “a way to bring public and private sectors together in long term partnership for mutual benefit”. (HM Treasury).

In South Africa, Treasury Regulation 16 of the public finance management act (PFMA) defines a PPP as a “contract between a public sector institution/municipality and a private party, in which the private party assumes substantial financial, technical, and operational risk in the design, financing, building, and operation of a project”. (National treasury’s PPP manual, 2004).

In conclusion, the central element represented in these definitions is cooperation; sharing of responsibilities, decision-making power and authority, sharing of risks and rewards/mutual benefit, pursuing shared or compatible objectives and joint investment. Achieving value for money, especially from the taxpayer’s perspective, is reflected as an element of PPP.

### **3.2.3 Evolution of public private partnerships**

Partnership is not a recent concept: it gained substance largely in the 1970s, particularly in the United States (US) with contracting out initiatives and in the United Kingdom. In both countries, its origins were associated with planning and urban development problems, where there were considerable shortfalls in finance.

The PPP approach became recognised worldwide as an effective way of delivering value for money public infrastructure and services following the introduction of the private finance initiative (PFI) during the nineties in the United Kingdom. Under the auspices of the PFI in 1992, a Conservative government began to tap the private sector to manage the building and operation of investments previously undertaken within the public sector (Terry, 1996). The PFI has been used to develop and deliver different types of infrastructure and services and now represent 10% to 13% of all UK investment in public infrastructure. Close to 100 PFI projects are initiated or completed per year (Deloitte Research, 2006).

### **3.2.3.1 *PPP development globally***

According to Deloitte Research (2006), the growing use of the PFI has inspired governments worldwide to adopt PPP arrangements, as governments recognised their value. The Australian government has used PPP to deliver several social infrastructure projects. Ireland has used them for transport infrastructure. In the Netherlands, social housing and urban regeneration programmes have been delivered through PPP arrangements. India is investing heavily in highways through PPP. Japan has roughly 20 new PPP in the pipeline. In Canada, 20% of new infrastructure are designed, built, and operated by the private sector. The US is a pioneer with contracting out and has started

experimenting with other forms of PPP and emerging democracies from central Europe are following suit.

### **3.2.3.2 PPP in developing countries**

PPP also play a significant role in the infrastructure development of developing countries. According to Deloitte, in Africa, between 1990 and 2004, approximately 14% of public sector infrastructure was provided through PPP, the most common sectors being water, energy, and transport. (Deloitte Research, 2006).

### **3.2.3.3 PPP in South Africa**

South Africa has had a sophisticated and well-defined PPP framework for the past ten years. In April 1997, the South African cabinet approved the establishment of an inter- departmental task team (IDTT), chaired by the department of finance, to initiate the development of a regulatory framework for PPP, and explore how PPP could improve infrastructure and service delivery efficiency. The cabinet endorsed the strategic framework for PPP in December 1999, and in April 2000, the national treasury issued regulations in terms of the public finance management act (PFMA) for PPP. A PPP unit was then established in the national treasury in the mid 2000 and in 2001 the treasury public private partnership manual was published.



South Africa's PPP projects include toll roads, hospitals, prisons, and office accommodation. To date there have been 20 PPP projects that reached financial close since 2001 and just one project has closed in 2010 – the Foreign Affairs head office new building. Industry practitioners have raised concerns about the slow deal flow in the South African PPP market.

#### **3.2.3.4 PPP adoption by sectors**

While initially focussing on economic infrastructure (multi-user facilities and services that are direct inputs in the chain of production, including water, waste and transport facilities), PPP have evolved to include the procurement of social infrastructure (large scale, multi-user services and facilities that are not direct inputs in the chain of economic production, including health care, education, and public housing) (Susiwalati & Armitage, 2004), depending on the maturity stages of each country.

There is an increasing trend towards a search for new formulations combining public with private activity, in order to respond better to the demands arising in a very large number of domains; namely, social housing, urban renewal and inner city programmes. According to a study by Deloitte (2006), in most advanced national economies, new forms of PPP are continuously emerging, and the existing ones are being tailored to the needs of different sectors

The next section contains a short overview of the main types of PPP ranging from the least sophisticated modes of private sector involvement to the most complex forms of PPP.

### **3.2.4 The value of Public Private Partnerships**

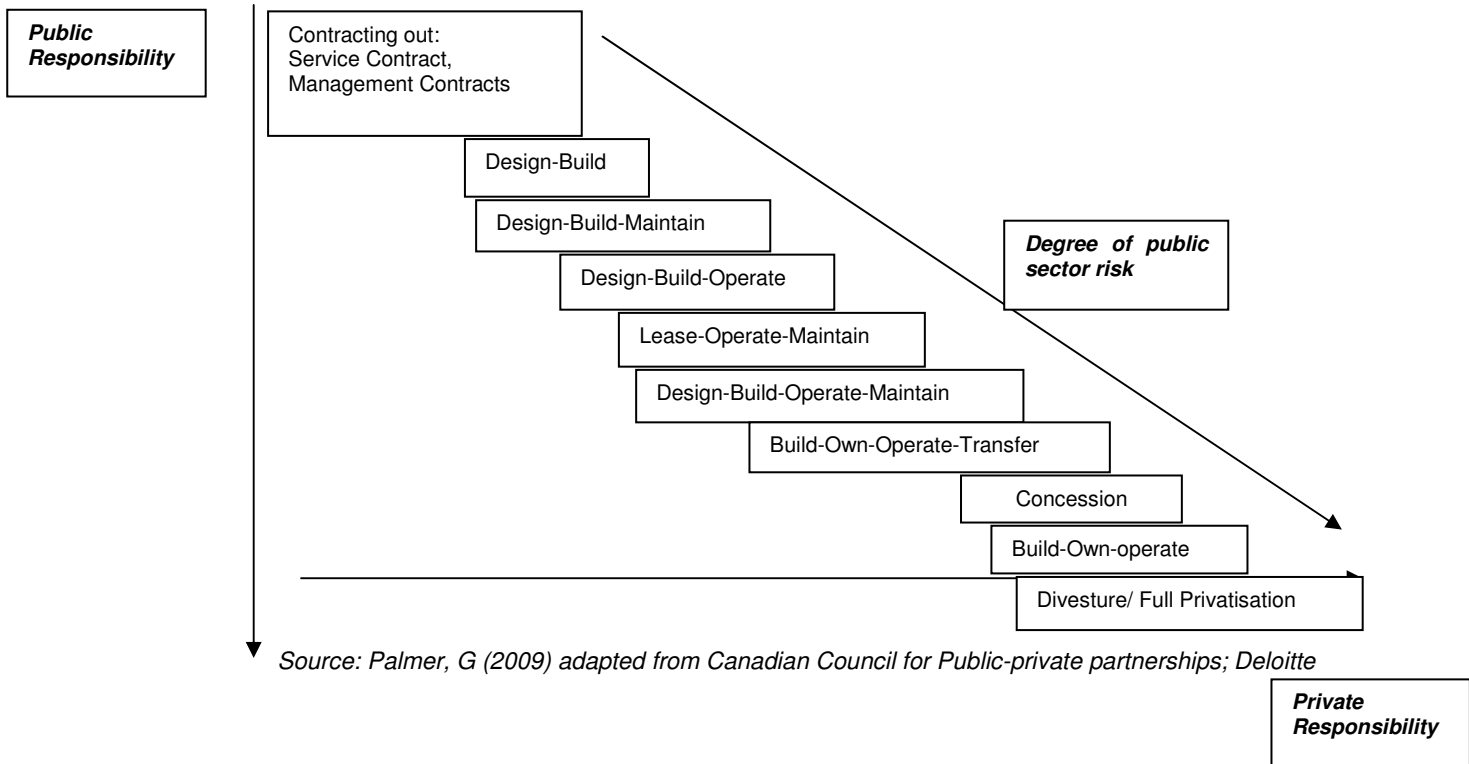
PPP have emerged as an important model governments use to close infrastructure gaps as it offers several benefits to governments trying to address infrastructure shortages or improve the efficiency of their organisations. The key drivers of involving the private sector were (and are still) to address public sector budget deficits and to search for greater efficiency, creativity, satisfying growing demands and the expectation of new and upgrading of existing ageing infrastructure (Grimsey & Lewis, 2004).

### **3.2.5 Different types of PPP**

PPP are normally classified in a continuum that reflects the degree of private involvement. At one extreme is the public provision, where the public sector is fully responsible for all aspects of delivering public services; while at the other extreme, is the private provision, where the private sector assumes all those responsibilities. As the PPP move from the end of the purely public provision to the other, the degree of private involvement increases. These PPP also vary in terms of finance sources and ownership of properties. As the figure below

indicates, partnerships can range from being under the direct provision of the level of government involved in the partnership to complete privatization.

**Figure 3.2: The public-private partnership continuum**



Allan (1999) classifies types of PPP according to different partnership variants on a continuum that reflects the extent to which risk is being transferred from the public to the private partner. The continuum runs from a contribution contract with minimal risk transfer, to buy-build-operate (BBO) partnerships with a maximum or complete risk transfer. In between the two are several possible combinations of functions the private sector can undertake; design, build, finance, operate, maintain, own, transfer, lease, develop and buy.

The following table (Table 3.1) summarises the different PPP models and their main variants differentiated largely by the level of risk shifted to the private sector.

**Table 3.1: Elements of different types of PPP**

Element	Description	Out-sourcing	PFI	Concession	Lease	BOT
<b>Operation</b>	Operation of service	X	X	X	X	X
<b>Finance</b>	Capital investment financed by private operator		X	X		X
	Recouped by user charges			X	X	
	Recouped by contract from municipality	X	X			X
<b>Construction</b>	Construction of asset by private company		X	X		X
<b>Ownership</b>	Public during and after contract	X	X	X	X	
	Private during contract, public after			X		X
	Private indefinitely					

Source : Hall, D., de la Motte, R. Davies, S. (2003)

There is a range of other terms used to describe variations of the BOT, PFI concession type of PPP. These include:-

**Table 3.2: Types of PPP models**

Model	Description
Design, Build, Finance and Operate (DBFO)	A contract let under the principles of the private finance initiative whereby the same supplier undertakes the design and construction of an asset and thereafter maintains it for an extended period, often 25 or 30 years
Design and Build (DB)	A contract where a single supplier is responsible for designing and constructing a built asset
Build Own Operate Transfer (BOOT)	Projects of the Build-Own-Operate-Transfer (BOOT) type involve a private developer financing, building, owning and operating a facility for a specified period. At the expiration of the specified period, the facility is returned to the Government
Build Own Operate (BOO)	The Build-Own-Operate (BOO) project operates similarly to a BOOT project, except that the private sector owns the facility in perpetuity.

A typical PPP in South Africa, takes the form of a design-build-finance-operate (DBFO) model, where the private sector designs, finances and constructs the elements of the project under a long term lease, and subsequently operates the facility during the term of the lease.

The choice of a model often depends on the market and type of project, and is guided by the right structure to create value for money (National Treasury's PPP manual, 2004). The sector of application also influences the choice of a

model, as each sector faces different challenges across each phase of the PPP life cycle. Furthermore, a correct evaluation of each party's abilities and management capacities has a direct impact on the choice of the PPP model and on the likelihood of success or failure of the project (Li, Akintoye, Edwards, and Hardcastle, 2004).

The selection of a model will, therefore, be guided by many factors, including the project objectives and requirements, the asset type, the abilities of the parties involved in the project, and their abilities to manage the different risks. Some areas will be better suited for risk transfer to the private party than others, while some risks would be retained by the public sector.

The bottom line: PPP policies, approaches, and political strategies must be tailored to the unique characteristics of each individual sector (Deloitte research, 2006)

### **3.2.6 Theoretical justification for PPP**

This section presents and reviews the current thinking of literature on the theoretical justification for PPP.

Public and private sector response to PPP has so far been mixed worldwide. Some participants actively welcome the policy (Middleton, 2000), while other reactions have been largely negative (Owen & Merna, 1997). The attractive and

negative factors of PPP have been discussed by many previous researchers and this section reviews some of the work:

### **3.2.6.1 Advantages**

Proponents of PPP often point to the financial benefits of partnerships. They argue that PPP have greater potential in delivering high quality services at lower costs than those available through public investment and government provision of the same services (Moszoro & Gąsiorowski, 2008; Hemming, 2006). The lower costs result from the fact that public funding is used to leverage private involvement, which is then being matched and bettered by private investment; the higher quality is achieved by bringing together the strengths from both the public and private sectors (Hemming, 2006).

Another financial benefit of PPP is their capacity to resolve the large cost overruns and delays in traditional public procurement that has been demonstrated in several studies (Li & Akintoye, 2003; Flyvbjerg, Holm & Buhl, 2005, Ho, 2006). As the private sector brings commercial discipline into public projects, the risk of overruns and project delays can be drastically reduced. This benefit is enabled by the appropriate financial analysis that often goes into PPP (e.g. Akintoye, Hardcastle, Beck, Chinyio, Asenova, 2003; Norwood & Mansfield, 1999; Huang & Chou, 2006; Saunders, 1998).

### 3.2.6.1.1 **Efficiency gains**

Mackintosh, (1992) and Kumaraswamy, Zheng, & Palaneeswaran, (2002) have suggested that partnering can also raise effectiveness in the development process in that it leads to the pooling of expertise, resources and skills in a collaborative fashion rather than a purely competitive one, bringing together the strengths of diverse backgrounds for the public good. This is particularly true for large infrastructure projects as the synergies that can be obtained lead to comprehensive solutions and benefits that would not be achieved with one partner working alone. Therefore, PPP create an enhanced partnership between the public sector and the private sector (Erridge & Greer, 2002; Ysa, 2007; Zhang & Kumaraswamy, 2001; Zhang, 2004a,b).

### 3.2.6.1.2 **Better risk management**

Another frequently cited advantage in the PPP literature is that the public sector and private sector can share risks at different stages (e.g. Grimsey & Lewis, 2002; Li, Akintoye, Edwards, and Hardcastle (2005).; Shen, Platten & Deng, 2006.). These studies found that partnerships achieve better value for money because it becomes possible to allocate particular risk to the partner best able to manage that risk. The opportunity for efficient risk allocation is dependent largely on the type of project delivery option chosen. Generally speaking, the private sector tends to take a more robust approach towards identifying and



pricing risks than the public sector. This suggests that both the private and public sectors need to have a better understanding of these risks. A fair and an equitable allocation of various risks is vital to PPP success and enables the project to generate better outcomes (Chan, Chan, Ho, 2003, Li, 2003; Xenidis & Angelides, 2005; and Zhang, 2001). This is particularly challenging as, in fact, most stakeholders are not willing to accept excessive risks.

### **3.2.6.2 *The disadvantages of PPP***

Offsetting the potential advantages of PPP are a number of factors that need to be carefully considered:

#### **3.2.6.2.1 Transaction cost: time, effort and cost**

High transaction costs arising from complex processes and the need for highly skilled resources to develop, manage, and monitor projects are a common factor across large PPP, at least during initial projects. A recurring theme which all parties involved in PPP agree upon is that to get the best outcomes from a potential PPP the public sector must be adequately resourced, both in terms of financial capability and human resources at the project development, evaluation and tendering stages. Under resourcing at this stage will expose the public sector to the risk of losing the potential benefits which a PPP might deliver, (e.g.

through choosing a suboptimal procurement strategy, or failing to successfully transfer risks associated with benefits).

It is worthwhile to note that, PPP projects may incur higher transaction costs than those under conventional public sector procurement; due to the complex arrangements as PPP involve many parties with conflicting objectives and interests. Mostly, PPP projects often require extensive input of expertise and high costs and involve lengthy negotiations. According to researchers (e.g. Grimsey & Lewis, 2004; Li, 2003; & Zhang, 2001) the potentially high transaction costs may have a negative impact on the objective of securing the best value.

Furthermore, despite the many benefits, PPP are not considered by some scholars and industry practitioners as a solution for all infrastructure projects, as it is too complex and costly for small projects. For example, Sharp & Tinsley (2005, p.6) state that PPP involve considerable administrative cost and should be used for procurement of large and long term projects to justify the additional cost.

Kumaraswamy & Zhang (2001) presented several cases of BOT ventures that ran into problems due to cost overruns, unrealistic prices and income projections, and legal disputes between operators and the government. This suggest that a PPP is one of the most complex form of procurement, as it brings about complex arrangement of different parties with competing objectives. PPP

involve a great deal of legal structuring and documentation to deal with potential disputes amongst PPP parties, a “water-tight” legal framework is still lacking (e.g. protection of public interests versus legitimate rights of private sector) Grimsey & Lewis, (2004). Without a well established legal framework, disputes are inevitable (Grimsey & Lewis, 2004 and Li *et al.*, 2005). Still some countries do not have a well established legal framework for PPP projects and the current legal framework is only supposed to deal with the traditional command and control model.

#### 3.2.6.2.2 **Public accountability and democracy**

Flinder’s (2005) work suggests that, in addition to the financial, administrative, and technical aspects of PPP, partnerships raise a host of political issues that the wider literature in the area has tended to neglect. While he acknowledges that there is potential for short term efficiency gains in some policy areas, he questions the unintended long term costs on public accountability and democracy.

PPP projects may fall apart due to failure on the part of the private sector participants. Due to a lack of relevant skills and experience of project partners, PPP projects are more complex to procure and implement.

### 3.2.6.2.3 Political factors

Practitioners have indicated stakeholders' opposition and public opposition have contributed to a failure of PPP projects (Algarni, Arditi, Polat, 2007). PPP in public projects typically involves political and social issues like land resumption, town planning, employment, heritage and environmental protection. These could result in public opposition, overblown costs, and delays to projects..

An unattractive financial market (e.g. politically unstable or high interest rates) is often a negative factor to PPP success.

When assessing these advantages and disadvantages of PPP, one realises that the determinants of PPP mainly relates to the conditions in the host country.

### 3.2.7 Summary

PPP have generally proven to be an effective infrastructure delivery tool, but a number of projects, nevertheless, have failed to live up to expectations. Grimsey, (2007) contends that more PPP projects have been successful compared to the few cases of failure. What is shared in the literature is that there is a clear benefit achieved through the risk transfer and the involvement of the private sector in infrastructure delivery. This section of the literature review highlighted that it is generally well accepted that PPP are a useful and essential mode of infrastructure service delivery.

Although the wider scholarly debate on PPP does raise some real concerns over the long term effectiveness of PPP, under the current set of circumstances, partnerships within the private sector are an option worthy of consideration to help address the housing shortages. While research on the topic is limited, there are many reasons to believe that partnerships can offer one way forward in the provision and management of affordable housing. The next section reviews the use of PPP in social housing and the challenges pertinent to the sector, and draws implications.

### **3.3 Public private partnerships (PPP) in social housing**

#### **3.3.1 Introduction**

Governments that have multiple, successful partnerships recognise that each sector carries with it different challenges across each phase of the PPP life cycle (Deloitte Research, 2006). PPP policies, approaches, and political strategies must, therefore, be tailored to the unique characteristics of each individual sector. This section discusses, through the literature, the potential role of PPP in housing, identifying supports and constraints, examining the rationale and development of PPP in affordable housing, and outlines some of the opportunities and challenges particular to this sector. International experience in this area is highlighted, and the lessons and implications, and key components of these successful partnerships are identified. These were used as a discussion point with key stakeholders in the empirical phase of the study.

#### **3.3.2 The opportunities and challenges of PPP in social housing**

PPP in housing are still emerging in developing countries and the extent of their use has depended, amongst other things, on the economic strength, prevalent political environment and housing tradition of a particular city (Sengupta, 2006).

Internationally, there has been a shift from governments being the direct provider of urban housing, given the limited scale of production achieved and

apparent financial constraints of governments (Keivani & Werna, 2001). These constraints resulted in gross incapacity of governments to deliver, mainly because the whole approach lacked a sound economic base due to the level of subsidies involved and failure to recover costs (Sengupta, 2006).

The emergence of PPP is rooted in the enabling approach, where focus shifted the direct provision of housing by governments, to a focus on governments providing an enabling environment for low income housing provision by other parties. The primary objective of the enabling approach has been to improve the efficiency of the housing sector by the public sector concentrating on eliminating constraints on both the supply and demand sides. The World Bank (1993) and the UNCHS (1992) have suggested that, in operational terms, enablement will often take the form of partnership arrangements that bring together government policy makers, government agencies, community based organizations, NGOs, private builders, and/or households.

Researchers have also explored the possibility of increasing the supply of low income housing by stimulating private sector involvement in affordable and low income housing projects (Moskalyk, 2008; Susilawati & Armitage, 2004; Brown, Orr & Luo, 2006 and Scanlon & Whitehead, 2007). However, literature specific to PPP in housing in developing countries, is relatively limited.

The potential value of social housing PPP is the increase in the availability of finance for housing, and thereby increasing the supply of housing from present

levels. According to research by Canadian Mortgage and Housing Corporation (CMHC) 1999, PPP affords efficiency gains; lower costs, quicker completion and higher service levels due to a number of factors; namely, performance-based contracts, risk transfer to private-sector providers, integration of the various phases of a project, and the requirement that the private partners finance most of the costs of the project. PPP accelerate project development and save time in delivering the project (Iacobacci, 2010). PPP can also lead to increased competition and, therefore, efficiency in the housing market.

While PPP have found their way into urban development, they are not without complexities. These issues, while not necessarily unique to social PPP, are perhaps more acute than for economic PPP (Susilawati & Armitage, 2004)

Some of the complexities and challenges in social housing PPP are as follows:

- The main challenge in social housing PPP is the conflicting commercial and social focus of the different parties. The challenge here is to ensure sufficient revenue streams from the project to attract private sector involvement in a sector where affordability is problematic.
- The credit risk profile for housing PPP also varies considerably from that of other PPP. Social housing projects are characterised as generally being smaller in scale than economic infrastructure projects (e.g.



motorways, bridges, tunnels, etc.) and, by their very nature, also tend to be complex, particularly in terms of ongoing involvement with tenants (Susilawati & Armitage, 2004). Thus, private-sector bidders for social housing PPP projects are often presented with a situation where the financial rewards are less and the operational demands are more complex than for other infrastructure PPP projects.

- The transaction costs of developing and monitoring PPP contracts are normally higher than for conventional procurements. In the case of a housing PPP, the high bidding cost and the high operational costs (i.e. financing, risk and procurement costs) can question the financial viability of a PPP in social housing. For small scale projects, transaction costs can typically be high, particularly for cases where the procurement process is long and complicated. The capital value of individual housing projects may, therefore, not attract sufficient private sector interest.

In summary, PPP present both opportunities and challenges. The experiences of developed countries, however, demonstrate that these challenges can be surmountable. The next section assesses the experiences of two trailblazers in PPP (the United States and the United Kingdom) in order to identify key attributes and the success factors of PPP in social housing.

### **3.3.3 Experience in the provision of social housing in other countries**

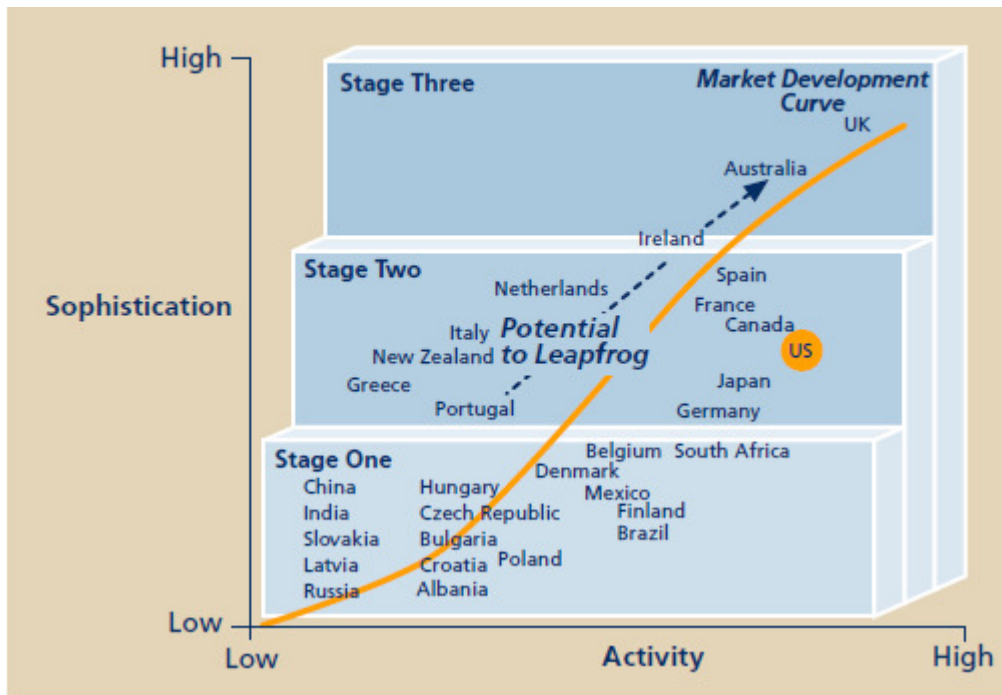
#### **3.3.3.1 Introduction**

The purpose of this section is to provide an overview of the different models that have been used successfully in other countries for social housing. This will assist with the identification of a way forward for partnerships in the social housing in South Africa.

Comparisons of housing models across different countries are widely accepted as difficult, because of the need to take account of broader economic and social factors. Whilst international experience in social housing PPP cannot be directly replicated to the South African housing conditions, governments at earlier stages of PPP development could benefit from the opportunity to learn from the trailblazers who have moved to more advanced stages.

Countries remain at vastly different stages of understanding and sophistication in using innovative partnership models (Deloitte Research, 2006). Each country, and even individual states and localities, takes its own path in developing PPP. Many factors play a role in development including local geography, political climate, the sophistication of the capital market, the forces driving formation of partnerships and the factors enabling their creation. Nevertheless, three distinct stages of PPP maturity can be observed across the world (See figure 3.3).

**Figure 3.3: PPP market maturity curve**



Source: Deloitte Research, 2006.

The United Kingdom, Australia, and Ireland, for example, are at the highest stage of development in the PPP market maturity curve (Deloitte Research, 2006).

For countries, which seek to expand their use of PPP into new sectors, it is important to develop a deep understanding of the challenges and potential solutions particular to each infrastructure area. To that end, this section, therefore, takes advantage of the learning curve through which PPP in social housing have passed through in the UK and the US, and gives a brief overview

of the different models that have been used for affordable housing and identifies the key components to successful partnership arrangements.

#### **3.3.3.1.1 The United Kingdom experience**

The United Kingdom (UK) is, according to a study by Deloitte (2006), a leader in the use of PPP. In the UK, housing in the social sector has depended on the private sector to supplement public funding by introducing a housing private finance initiative (PFI), to encourage partnerships between the private and public sectors (Moskalyk, 2008).

#### **3.3.3.1.2 The context in which PPP have emerged**

Given an acute lack of public finance available for the repair, maintenance, and new provision of social housing stock, the UK government decided to develop pathfinder projects to promote PFI (PPP) in social housing. In 1998, eight local authorities were selected as pathfinders for PPP /PFI housing projects. These authorities were selected to explore the potential of PFI/PPP in social housing. The pathfinder PFI schemes covered a range of different types and number of dwellings, which included traditionally, built estates, modern high-rise tower and incorporated refurbishment projects and new build construction projects.

### 3.3.3.1.3 Features of the PPP approach

Under the PFI, local housing authorities award a long term contract to a private consortium, which is usually made up of a bank, a housing contractor, and a housing association. The contractor provides a number of housing services, including repairs and maintenance. Among the main goals of the housing PFI are to provide an affordable way to attract investment to social housing, to provide significant improvements to housing conditions and to maximize the value of public money by ensuring a transfer of risks from the public to the private sector, which may be better able to understand and manage both short term and long term risks (Moskalyk, 2008).

### 3.3.3.1.4 Funding framework

Resources to support the capital element of the projects were provided by central government in the form of PFI credits that deliver additional subsidy to housing revenue accounts, held by local authorities. The revenue element of projects was supported by the local authority via the management and maintenance allowance

### 3.3.3.1.5 Lessons

Through the pathfinder projects, UK local authorities have attempted to learn when and where to apply PFI and how best to set out and manage PFI for social housing. Briefly, UK experience drawn from pathfinder projects indicate:

- PFI/PPP should be considered the preferred option when the alternative methods of securing investment are either unviable economically or unacceptable to tenants
- PFI/PPP projects were considered to deliver added value over longer contract periods, because PFI is thought to be the only investment mechanism that 'locks in' investment to maintain a specified output standard for housing stock
- The commitment of central government, in terms of policy and regulation, was necessary to provide confidence to investors
- Additional government resources were focused on an objective of developing standards and templates for, and stimulating the emergence of a PFI supplier market

### **3.3.3.2 *The United States experience***

In the United States (US), PPP are the country's main source of social housing, and there are myriad examples of partnerships that have emerged in the housing policy sector (Moskalyk, 2008). A wide array of supportive financing mechanisms have been put in place by governments in the United States, which has stimulated the production of social housing through PPP.

### 3.3.3.2.1 **Context in which PPP have emerged**

The emergence of the partnership approach in producing affordable housing began in the early 1980s due to a significant reduction in new funding. Prior to the 1980s, federal housing subsidy programmes in the United States were the primary vehicles to develop affordable rental and homeownership opportunities. In the early 1980s, the U.S. department of housing and urban development's (HUD) budget authority for new housing commitments was cut by over 70 percent. At the same time, state and local governments were also under budget cutting pressures, which limited their ability to fill the gap.

### 3.3.3.2.2 **Features of the PPP approach**

According to a study by the Canadian Mortgage Housing Company (CMCH), (1999) there is diversity in the nature of arrangements used in the USA. More partnerships in the US are rooted in the non-profit sector. An apparent “system-wide”, public-private partnership (PPP) approach, involving the widespread participation of corporations, philanthropies, foundations, lenders, financial investors, and the non-profit sector, has evolved to such an extent that this new paradigm has become almost the sole approach used to produce affordable housing. Many cities have established formal partnership agencies, autonomous from the local government, drawing on the expertise and financial participation of community and corporate partners. These autonomous and well-

resourced local PPP have proven to be extremely flexible and responsive in developing local programmes that meet local affordable housing need.

#### 3.3.3.2.3 Funding framework

A wide array of supportive financing mechanisms have been put in place by governments in the United States, which has stimulated the production of social housing through PPP. A key feature of the US partnership model is that most of the mechanisms focus on the financing aspect of the project or partnership. There is, however, a reliance on mechanisms that reduce debt costs so that projects are viable without the need for ongoing subsidy assistance to reduce rents and increase affordability, where there is low cost or no-cost finance.

The United States have historically incorporated a wide variety of programmes and subsidy techniques to encourage local communities and partnerships to support affordable housing. The programmes in place include a housing block grant provided to state and local authorities, effective interest rate subsidies provided through tax exempt bonds, mortgage insurance and guarantee programmes, regulatory influences on mortgage capital, and state and local financial support mechanisms such as housing trust funds, which dedicate a source of public revenue for affordable housing projects (Lea & Wallace, 1996). The most notable source of government funding for social housing in the United States comes from the low income housing tax credit (LIHTC). This programme provides tax credits to local non-profit housing authorities that can then sell the



credits to private investors for cash; the private sector in turn uses the credits to reduce their taxable income (P3 Advisors Inc., 2008: 20). Affordability is pursued by minimising debt service costs so that the break-even rent is relatively affordable and the project is viable without the need for ongoing government subsidy assistance to reduce rents to affordable levels (CMCH, 1999)

### ***3.3.3.3 Implications drawn from the experience of other countries***

The path to successful PPP projects is complex and time consuming, and involves significant expenditure. No example has fully satisfied every success criteria. In general, the experience of various countries suggests that success in terms of the right quantity of high quality, sustainable housing cannot rely solely on the adoption of PPP strategies. The design of PPP contracts involves a number of key decisions in areas such as affordability, risk transfer and value for money (PPP Manual, 2004). A careful consideration of the value for money drivers is likely to enhance the possibility of PPP solution becoming a viable alternative to traditional methods of service provision. It is realistic to suggest that the potential for success is influenced by the economic, political and cultural circumstances of the specific country in question.

However, there are key strategies that can be learnt from experiences of advanced economies that have contributed to the growth and viability of social

housing. The next section details the different attributes and implications for South African housing PPP.

### 3.3.3.3.1 Key components of successful social housing PPP models

Identifying key components of successful partnerships will be of assistance to decision makers in both the public and private sectors by making explicit the key components that will lead to successful adoption and implementation of PPP in social housing.

The following are some broad characteristics of the US and UK funding framework that illustrate different approaches for providing housing:

UK	US
<p>Social housing supply is funded through a debt/equity model whereby housing associations leverage private finance to grow. The United Kingdom's regulatory model and rental framework that enables providers to generate sufficient rent revenue to support debt are the key factors in encouraging private sector investment in social housing. (Lawson &amp; Milligan, 2007)</p>	<p>The US government has historically had minimal involvement in the provision of affordable housing. (Lawson &amp; Milligan, 2007)</p> <p>The Low Income Housing Tax Credit scheme is the primary mechanism to increase the supply of affordable housing in the US.</p>
<p>The UK instruments include: low site costs, mixed income, mixed use and cross subsidies</p>	<p>The US instruments are focussed on: reducing project costs by accessing a high proportion of zero or low cost financing , and minimising debt cost</p>

#### *3.3.3.3.1.1 Partnership structure*

The partnering arrangement would include the public sector, the private for profit and not for profit entities and state developmental finance institutions.

#### *3.3.3.3.1.2 Funding framework*

The funding should thus comprise a mix of subsidies, loan finance and grants, private equity, commercial debt finance loans from private sector finance institutions and other state development finance institutions at subordinated low interest or zero interest loans.

#### *3.3.3.3.1.3 Targeted market*

The international literature on low income housing provision has given priority to partnerships that entail the construction of mixed income housing estates. The idea is that the latter would subsidize the former (Susilawati and Armitage, 2004). The profit from the higher end product subsidises the low income housing which demonstrate the dual roles of the associations. It is, therefore, recommended that the mixed housing developments provide wider housing options to clients over their life cycle.

#### *3.3.3.3.1.4 Land acquisition*

PPP schemes should preferably include local authority land at no cost to enhance the financial viability of the project. The contribution of land by local

government has proved instrumental in the success of many social housing projects.

#### *3.3.3.3.1.5 Types of projects*

In addition to being used for new projects, PPP can also be used for existing facilities including inner city, residential refurbishments, conversion of offices to residential units and Greenfield developments for rental accommodation. PFI was considered appropriate for varied types of stock in the case of either refurbishment or new build construction

#### *3.3.3.3.1.6 Transfer public stock to SHI to build an asset base*

Transferring title in public housing stock to SHI is a key policy lever being used by the United Kingdom, to increase the scale and capacity of housing providers to improve their viability, sustainability and growth prospects. All properties owned by the states are transferred with minimal or no cost. This allows the SHI to

#### *3.3.3.3.1.7 Undertake some commercial activities*

SHI can increase revenues by engaging in some commercial activity that achieves market profits. The proceeds of these activities would subsidise its core social housing market. This strategy would overcome the viability and growth constraints faced by the organisation due to limited rental returns.

For example, in the United Kingdom, there has been a significant increase in social housing providers redeveloping and selling property to increase their surpluses.

#### *3.3.3.3.1.8 Lower the cost of finance*

Lowering the cost of finance via for example, government guarantees, can free-up capital and allow the property owner to focus on tenant needs. This option is a more direct avenue for property owners to access funding and negotiate with banks for terms that are more favourable.

### **3.3.4 Summary**

This section discussed through literature the potential role for PPP in housing, identifying supports and constraints, examining the rationale and development of PPP in affordable housing, and outlines some of the opportunities and challenges particular to this sector. The main opportunities identified is the enhance source of funding. However, PPP in social housing are very complex. International experience with social housing PPP shows that there are a myriad of models that can be used effectively to meet housing challenges.

## **3.4 Conclusion of literature review**

The primary argument for PPP remains the notion of “value for money”. Underlying that notion is the theoretical justification that market competition and

better incentives (solving the principal-agent problem and the accountability problem) will create public services that are timelier and as good as or better than are now provided by the public sector. These advantages arguably outweigh the likely increase in transaction costs involved in PPP.

PPP can provide public officials and managers with an optional approach to the production of cost-effective government services. From the above, it is clear that while Public Private Partnerships have been covered in various depths, there is a need to document what is happening in social housing in South Africa, and to test the perceptions of stakeholders to gain insights into the perspectives into the suitability and attractiveness of the PPP framework. Much has been contended in this matter, but gaps exist as to what had been empirically ascertained, hence, the need to investigate this. An opportunity, therefore, exists to explore the suitability of the PPP in social housing.

## 4 CHAPTER 4: RESEARCH QUESTIONS

The following questions were asked for this research:

### 4.1 Research question 1

*What are the challenges in social housing delivery?*

Research question 1 was aimed at understanding the challenges specific to the sector that are pertinent to the growth and viability, and subsequently the formation of PPP in this sector.

### 4.2 Research question 2

*Is the PPP an appropriate delivery mechanism for the accelerated delivery of quality and sustainable social housing in South Africa?*

Research question 2 aimed to assess the suitability of PPP by identifying the benefits and complexities with implementation and key success factors for social housing PPP.

### 4.3 Research question 3

*What are the key components of a partnership?*

This question aimed to identify model attributes that would be used as building blocks for social housing PPP in South Africa.

## **5 CHAPTER 5: RESEARCH METHODOLOGY**

### **5.1 Introduction**

This chapter discusses the research methodology used in this study.

The review of literature on the UK and the US experience in PPP in social housing, including the opportunities and challenges posed by PPP in general provided insights into how this approach can be applied to social housing. From this theoretical base, key components of successful PPP models were identified, which served as a discussion point in in-depth interviews with current and future stakeholders involved in the delivery of social housing and public private partnerships. Their perceptions about the suitability and effectiveness of the PPP in facilitating increasing delivery and quality of social housing in South Africa, were obtained in a series of in-depth interviews. Based on the findings, the recommendations that would support future programme initiatives that encourage PPP based social housing in South Africa, were formulated.

### **5.2 Research design**

The research was descriptive and qualitative in nature. Zikmund (2003) described descriptive research as that which is designed to describe characteristics of a population or a phenomenon. In this case a Public Private



Partnership. According to Zikmund (2003), descriptive research is conducted when there is some previous understanding of the nature of the research problem. Whilst extensive research has been done in understanding the opportunities and risk of PPP in other sectors and countries, the suitability of the model in its current form has not been explored in South Africa.

The research had the following phases:

- *Phase I: Literature review and identification of key components of PPP models.* The first phase of the research, the literature review, sought to formulate the characteristics of PPP in social housing, documenting what has been done in other countries in order to identify the key conditions for success and the factors that influence the attractiveness of PPP in social housing. Key parameters and principles of social housing PPP were extracted from the literature review.
- *Phase II: In-depth Interviews*

The next phase involved in-depth interviews with a distinctive group of stakeholders, to assess their perceptions concerning the appropriateness of PPP in social housing.

### **5.3 Unit of analysis**

Zikmund, (2003) stressed that determining the unit of analysis should not be overlooked during the problem definition stage of the research. The unit of analysis in this study was the Public Private Partnership, as the research analysed its suitability in social housing delivery.

### **5.4 Population and sample**

#### **5.4.1 Population of relevance**

The population for this study consisted of four distinctive groups of populations, which are representatives of major role players in the delivery and management of existing and/or future social housing, and those experienced in PPP .

These key stakeholders are the public sector, private non-profit organisations, the private sector, consultants and researchers involved in social housing (Table 5.1).

The four distinctive groups were identified as the populations from which the samples were to be extracted for the face-to-face, in-depth interviews.

**Table 5.1: Population**

No	SECTOR	SUBGROUP	No of organisations
1	Consultant/ Researcher	Consultant/ Researcher	3
2	Private for profit	Financier	3
3	Private for profit	Property Management/ Development	2
4	Private not for profit	Social Housing Institution	3
5	Public	State Development Finance Institution (DFI)	3
6	Public	Government	1
<b>Total</b>			<b>15</b>

## 5.4.2 Sampling method and size

### 5.4.2.1 Selection of interviewees

Sampling was focused on gathering qualitative data from the distinct groups identified above, and samples were selected using non-probability judgement sampling. Zikmund (2003) described this type of non-probability sampling as: “that, which is employed to serve a specific purpose, when the researchers use their judgement to select the sample based on appropriate sample characteristics.” In this case, judgment was based on the respondents’ roles and responsibilities in social housing delivery and experience with PPP. The individuals targeted, were carefully selected as being knowledgeable individuals both directly and indirectly involved in the industry investigated.

The respondents had to meet the following criteria:

- Senior managers who possess known or demonstrable experience and expertise in social housing, experience on conducting social housing research, or have followed closely the development of social housing
- They had to possess adequate knowledge in the area of PPP or hands-on experience with PPP projects, experience in conducting PPP research, or have followed very closely the development of PPP.

While this type of sampling can afford the guarantee of meeting specific objectives, the disadvantage is that, based on the researcher's beliefs, bias might be introduced which can make the sample unrepresentative (Zikmund, 2003).

Proportional, stratified sampling was used to allow for triangulation between the groups where the members of the population were grouped into relatively homogeneous subgroups to check commonalities or differences of the views of the different stakeholders based on their population elements. This was done to ensure that balanced views were obtained, with a fair representation of all stakeholders. The rationale for the various viewpoints types was to gain insights from the private sector perspective, the public sector perspective, and the private non-profit sector perspective.

#### **5.4.2.2 *Number of interviewees***

The sample size was based on achieving a reasonable sample that the researcher could have access to. The target composition was a fair representation of stakeholders that would be involved in a typical PPP, as shown in the respondent list in Appendix A. Fifteen in-depth interviews were conducted in this study comprising as illustrated in table 5.1:

An email was sent to all potential stakeholders requesting their participation in the study, followed by a phone call.

### **5.5 Data collection and research instrument**

Given the nature of this study, this research required face to-face, in-depth interviews with the three sample groups in order to seek answers to the research questions in Chapter 4. Data was collected in one-time, individual, semi-structured interviews. The interviews were conducted with each respondent for about an hour. The main advantage of the one-to-one interview was the ease in transcribing the information, and the ease to control.

The main objectives of the interviews were to obtain a comprehensive picture of the major players' roles and their opinions on the possibilities of using PPP for social housing provision and management by determining their keenness in this arena. The research further established their perceptions and opinions on public private partnerships in social housing provision.

The research questions were posed to the stakeholders and the key components of a partnership model were used as a discussion point, allowing for ease of data collection. The researcher listened for emerging themes and coded the data. The advantage of this research technique, according to Zikmund (2003) is that face-to-face interaction assists the researcher to obtain complete and precise information. According to Denscombe (2007), face-to-face contact also offers means of immediate validation of data. The response rate for this approach is also better than other methods.

All interviews were tape recorded and transcribed verbatim for accuracy. The advantage of the audio recording is that it offered a permanent record and one that is complete in terms of the speech that occurs, and can be checked by other researchers (Denscombe, 2007).

However, the disadvantage is that it only captures speech, and misses non-verbal communication and other contextual factors. To that end, during the interview, the researcher captured detailed written notes, which noted any non-verbal cues in order to ensure that the information was properly documented.

### **5.5.1 Semi-structured interview guide**

An interview guide is included in Appendix C. The interview guide was designed in three sections, linking back to the main research questions in Chapter 3 as mapped in Appendix B.

## 5.6 Procedure for data collection

### 5.6.1 In-depth interview design

An interview is a purposeful discussion between two or more people (Kahn and Cannell, 1957, p149 cited in Marshall and Rossman, 2006, p80). An in-depth interview is an open ended, discovery-oriented method and the goal of the interview is to deeply explore the respondent's point of view, feelings, and perspectives (Guion, 2006). The in-depth interviews are structured in a way that encourages a conversation focusing on a number of themes with the intention of piecing together a puzzle (Mason, 2002). In this research, a semi-structured, draft interview guide was prepared beforehand and it was designed to examine the perceptions, views and the stakeholders regarding the use of PPP in social housing. The interview guide had a clear list of issues that needed to be addressed and questions to be answered. The advantage of this was that the guide helped make interviewing a number of different people systemic and comprehensive by delimiting in advance the issues to be explored (Patton, 2002).

The framework of interview questions in Appendix C guided the conversation, with each question relating to the research questions outlined in Chapter 4. The questions were open ended with more emphasis placed on the interviewee elaborating points of interest (Denscombe, 2007). In-depth interviewing was focused on extracting the respondent's understanding, and views regarding the

use of PPP. The interviewees were referred to the key components of successful partnerships in order to validate the concepts and thinking emerging from the existing research and thus assess their preferences for social housing delivery. A probing interviewing technique was used to increase the richness and depth of the responses, and give cues to the interviewee about the level of response that is desired (Patton, 2002) of provided a detailed response, thus giving further clarity and understanding of the respondent's viewpoint.

### **5.6.2 Pre-testing**

Pre-testing of the interview process was conducted before the interviews allowing the achievement of a natural flow; a clearer understanding of the intensity of data collection and allowing the researcher to be comfortable with the interviewing and probing technique as well as the data capturing process.

## **5.7 Data analysis and interpretation**

According to Denscombe (2007), data analysis calls for a discovery of key components or general principles underlying a particular phenomenon so that these could be used to provide a clearer understanding. The collected data is separated into components and reduced to more manageable pieces to allow for interpretation and extraction of conclusions. In this study, the data was analysed across the specified samples groups and subgroups in order to identify common themes. The analytical method used in this study was a



combination of content analysis and comparative analysis. This entailed analysing the content to identify specific categories of information and themes. The raw data was then coded, and these codes were grouped into categories. The researcher then identified relationships between the codes or categories of data and the patterns within the data in order to develop generalised conclusions. The individual responses were then compared between the different subgroups.

## **5.8 Limitations of the study**

The following were the limitations of this research:

- Since the research used non probability sampling, the results were not be generalisable;
- There was a possibility of interviewer bias due to the researcher's personal perceptions, assumptions, and interpretation
- The research was highly dependant on the quality of the answers provided by the respondents during the interviews.

## **5.9 Validity and reliability**

Data validity in qualitative research refers to the accuracy and precision of the data in terms of the research question being asked (Denscombe, 2007). Given

the nature of this research, the potential for the researcher's bias due to personal perceptions and assumptions and interpretation existed, hence, the need for interpretative validity. This required the researcher to pay attention to the language and perspective of the respondents during the interview as opposed to the researcher's interpretation of the respondent's comments.

## **5.10 Conclusion**

The research drew insights from a number of academic studies, practitioner's views and experiences in other countries with regard to PPP in social housing and enhanced these to identify key model parameters that could be applied as building blocks in designing an effective partnership in social housing in South Africa.

## 6 CHAPTER 6: RESULTS

### 6.1 Introduction

This chapter describes the data gathered during the empirical phase of the study facilitated by 15 semi-structured interviews with major stakeholders in social housing.

The data collected from the interviews was analysed using content analysis and frequency analysis techniques in order to identify common themes. The content analysis was performed using a spreadsheet, where the answers from the four sample groups were captured against the relevant questions. The four subgroups were aligned next to each other in the spreadsheet and each interview answer was allocated a portion of the template. The emerging themes were captured and for each identified theme the number of mentions was tallied up utilising frequency analysis, and rank-ordered from highest to lowest and tabulated in tables for each of the questions. The data was assimilated into common themes across the four sample groups. In some cases, only the concepts that were rated highest were included. Approximately one hour of content analysis was utilised per interview.

The interview questions were directly linked back to the three main research questions. The mapping of the interview questions was as per Appendix B.

The results are presented separately for each of the three research questions, directly linking back to the responses of the interview questions. The research data is presented in Tables, Figures and in narrative format.

Research Question 1: Sector specific challenges: Interview Questions 1 to 4

Research Question 2: PPP in social housing: Interview Questions 5 to 10:

Research Question 3: Optimal PPP model attributes: Interview Question 11

### **6.1.1 Results from research question 1: sector specific challenges**

Research question 1 served to identify themes relating to the constraints in the growth of the sector. Respondents were asked questions 1 to 4 as shown in Appendix C and the resulting transcriptions were analysed into a frequency distribution by stakeholder. The emerging themes for Question 1 and 4 were aggregated into Tables 6.1, 6.2, and 6.3. Responses tended to be in complex, detailed and lengthy conversations. These were para-phrased into smaller sets of themes or conceptual phrases as indicated in the preceding Tables.

The responses to the specific questions asked, are presented in the tables and figures below:

#### **6.1.1.1 “What are the current challenges in social housing delivery?”**

The most significant challenges in social housing delivery are illustrated below:

**Table 6.1: Challenges in Social Housing**

Rank	Theme	Excerpts from the interview	Total Counts	%
1	<b>Business Model</b>	<p>"Affordability constraints in the targeted income band"</p> <p>"Ability to get the rentals to remain in the affordability band"</p> <p>"The funding gap - matching the product price to the funding source"</p> <p>"High cost of commercial finance"</p> <p>"Rising construction cost"</p> <p>The current subsidy system</p>	12	80%
2	<b>Access to finance</b>	<p>"Government budgetary constraints -The limited government funding available for social housing"</p> <p>"The bureaucratic process of applying and receiving government funding"</p> <p>"Inflexible subsidies"</p>	11	67%
3	<b>Land and buildings availability</b>	<p>"The unavailability of well located, serviced and affordable land"</p> <p>"The lengthy and bureaucratic process of unlocking government land and buildings"</p> <p>"The high cost of land and buildings"</p>	10	60%
4	<b>Regulatory and legislative environment</b>	<p>Balance between tenant and landlord rights</p> <p>The rules and regulations in accessing government funding are not flexible, monitoring and reporting requirements that are too onerous</p>	8	53%
5	<b>Service Delivery by municipalities</b>	<p>"The expensive services delivered by the municipalities"</p> <p>"The inefficient service delivered by local municipalities"</p>	8	53%
6	<b>Capacity Constraints</b>	<p>The ability of SHI to manage their product (rent collection, property management, governance)</p> <p>Balance sheet to leverage debt</p>	5	33%
7	<b>Tenant/ Community interaction</b>	<p>Moral hazards: the unwillingness to pay rent when government finance is involved</p> <p>Lack of knowledge about social housing as a tenure: the mistaken belief that units are rent-to-own</p>	3	20%
8	<b>Scale</b>	The volumes required to break even	2	13%

**6.1.1.2 “Is the private sector in your knowledge involved in social housing?”**

Forty-seven percent (47%) of the respondents believed that the private sector was involved in this sector, whilst the majority were of the opinion that the private sector was not extensively involved. Responses were varied according to the involvement of the private financiers and property managers/developers.

**6.1.1.3 “What, in your opinion, are the constraints or factors that deter the private sector from participation in social housing?”**

The following Table illustrates the most common constraints and factors that discourage private sector participation in social housing.

**Table 6.2: Limitation factors for entering social housing investment**

<b>Rank</b>	<b>Theme</b>	<b>Excerpts from interviews</b>	<b>Total Counts</b>	<b>%</b>
1	<b>Business Model</b>	<i>"Ability to get the rentals to remain in the affordability band"</i> <i>"The funding gap"</i> <i>"High cost of finance"</i> <i>"Rising construction cost"</i> <i>The funding mix to make social housing work</i>	11	73%
2	<b>Conflicting objectives</b>	<i>Balancing the need of the private sector to generate returns to compensate for the perceived high risks and social focus</i>	11	73%
3	<b>Access to finance</b>	<i>"The bureaucratic process of applying and receiving government funding"</i> <i>"Inflexible subsidies"</i>	11	73%
4	<b>Regulatory and legislative environment</b>	<i>Balance between tenant and landlord rights</i> <i>The management of evictions in the context of legislation that criminalises the eviction of non-paying tenants without an eviction order:</i> <i>One-sidedness of rental laws</i> <i>The rules and regulations in accessing government funding are not flexible</i> <i>Uncertain policy and regulation</i>	10	67%
5	<b>Service Delivery by municipalities</b>	<i>"The expensive and inefficient services delivered by the municipalities"</i>	7	47%
6	<b>Operating environment</b>	<i>Moral hazards: the unwillingness to pay rent when government finance is involved</i> <i>Tenant participation</i>	7	47%
7	<b>Social housing as a form of tenure</b>	<i>"There is no consensus on what is meant by social housing particularly at the high end of the market"</i> <i>"A lack of awareness of developments in the social housing sector by the private sectors"</i> <i>"Social housing has 'not for profit' inference"</i> <i>"Social housing is seen as a market that is and should be catered for by government"</i>	6	40%
9	<b>Political interference</b>	<i>Inability of government to let the market go</i>	6	40%
10	<b>Capacity to deliver</b>	<i>Government lack of capacity to drive programmes</i>	6	40%
11	<b>Lending to reputable institutions</b>	<i>The inability of SHI to manage their product and lack of assets to leverage debt</i>	5	33%

#### **6.1.1.4 “Are the current incentives sufficient to attract private sector participation?” (Yes/No)**

Eighty-seven percentage (87%) of the respondents indicated that the current incentives were not sufficient to attract the private sector.

### **6.1.2 Results for Research Question 2: PPP in social housing**

The following sections illustrate the respondents’ views on the potential benefits and limitations of social housing PPP, and expectations of each stakeholder with PPP.

#### **6.1.2.1 “In your view, is the PPP, as regulated by the National Treasury, an appropriate sustainable delivery mechanism for social housing?”**

The majority of the respondents agreed with the concept of partnership. However, 88% of the respondents interviewed did not agree that it had to be registered or structured according to the National Treasury.

#### **6.1.2.2 “What in your view are the potential benefits of a PPP in social housing?”**

The following table illustrates the most common benefits of a PPP in social housing:



**Table 6.3: Benefits of social housing PPP**

<b>Rank</b>	<b>Benefits of PPP</b>	<b>Total Counts</b>	<b>%</b>
<b>1</b>	Alternate sources of funding	<b>13</b>	<b>87%</b>
<b>2</b>	Execution and implementation - Private sector expertise and efficiency in development and management of rental housing	<b>13</b>	<b>87%</b>
<b>3</b>	There is risk sharing across the sectors	<b>8</b>	<b>53%</b>
<b>4</b>	The private sector promotes efficiency, cost effective sustainability	<b>8</b>	<b>53%</b>
<b>5</b>	Commercial prudence, rigour and due diligence that is applied through PPP projects	<b>5</b>	<b>33%</b>
<b>6</b>	Innovation around better ways to utilise less public sector money	<b>4</b>	<b>27%</b>
<b>7</b>	Introduces the principles of value for money where public sector funds will be spent effectively	<b>4</b>	<b>27%</b>
<b>8</b>	Facilitates faster delivery and large scale developments facilitated by the funding from the private sector	<b>2</b>	<b>13%</b>
<b>9</b>	Synergies	<b>1</b>	<b>7%</b>
<b>10</b>	Can facilitate government flexibility around regulation	<b>1</b>	<b>7%</b>
<b>11</b>	Provides upfront capital for projects	<b>1</b>	<b>7%</b>
<b>12</b>	Gives the private sector an understanding of a significant part of the population that is not in the commercial market	<b>1</b>	<b>7%</b>
<b>13</b>	Enables the private sector to get involved in a sustainable way in housing people that would otherwise not be housed	<b>1</b>	<b>7%</b>
<b>14</b>	Neighborhood regeneration and urban transformation	<b>1</b>	<b>7%</b>

### 6.1.2.3 *“What is the role of the private-for-profit sector in meeting housing shortages?”*

The following were respondents’ answers to their opinion about the role the private sector can play in the social housing rental sector:

**Table 6.4: Role of the private sector**

Rank	Role of the private sector	Total Counts	%
1	Financing	9	60%
2	Execution and implementation	8	53%
3	Develop an inclusive and integrated society	2	13%

### 6.1.2.4 *What are the potential complexities with social housing PPP?”*

The following table illustrates the complexities in social housing PPP:

**Table 6.5: Complexities in social housing PPP**

<b>Rank</b>	<b>Complexities with social housing PPP</b>	<b>Total Counts</b>	<b>%</b>
1	High transaction costs especially for smaller projects	8	53%
2	Overly regulated process and the treasury rules, guidelines and process are a disincentive	7	47%
3	Political interference risk	7	47%
4	Very complex structures	6	40%
5	Making social housing profitable	6	40%
6	Rigidity of the generic model: Government is very rigid which creates difficulty when structuring deals	6	40%
7	Capacity of municipalities as implementing agencies	5	33%
8	Socio-political risks: People who live in accommodation that they believe is paid for by government believe that they are exempt from paying rent	4	27%
9	Lack of political will or government drive	4	27%
10	National Treasury's potential lack of understanding of social housing's complexities and softer issues	3	20%
11	Risk that the PPP could miss the social focus	3	20%
12	Driving the volumes and scale to make the business model work	2	13%
13	Fundamental distrust between the different parties	2	13%
14	Managing the relationships between the private sector and public sector	2	13%
15	Lack of critical experience in PPP , thus no confidence in the model	1	7%
16	Community building and tenant involvement	1	7%
17	The cost to the state of PPP are still going to be unaffordable and the subsidy requirement is not going to go away	1	7%

**6.1.2.5 “Do you think the South African conditions facilitate implementation of PPP in social housing??”**

Seventy-three percent of the respondents indicated that the current South African conditions would not facilitate successful implementation of PPP in social housing. The following factors would constrain the formation of PPP:

**6.1.2.6 “If No, please name the factors that would constrain the creation of social housing PPP?”**

**Table 6.6: Constrains to the creation of social housing PPP**

Rank	Constraints	Total Counts	%
1	Availability of subsidies	5	33%
2	Socio-economic factors	5	33%
3	Access to finance	4	27%
4	Uncertain regulatory and political environment	3	20%
5	Perceptions about the social housing market	2	13%
6	Negative investor sentiments	1	7%
7	Volatility of the labour market	1	7%

**6.1.2.7 What are the critical success factors for Social Housing PPP ?**

The following table illustrates the critical success factors to social housing PPP

**Table 6.7: Critical success factors for social housing PPP**

Rank	Success factors	Total Counts	%
1	Aligned interests	2	13%
2	Attract the private party with a long term view (Patient capital)	2	13%
3	Need institutions that are pragmatic, and less rigid to come up with innovative models	3	20%
4	Political support and commitment to facilitate (taxes, utilities, land availability)	6	40%
5	Need a regulatory environment that is stable	6	40%
6	Fair return on investment for private party	6	40%
7	Need the state to incentives rather than enforce.	4	27%
8	Government must come to the party with less onerous rules on subsidies	4	27%
9	Implementer has to have experience	3	20%
10	Provided that government can make decisions quickly	3	20%
11	Willingness of the public sector to trust the private sector	2	13%
12	Willingness to take risks	2	13%
13	Reputable partners: Dealing with not for profits that are solid, regulated some way, have capacity to manage,	2	13%
14	Flexibility	2	13%

### **6.1.3 Results for Research Question 3: Key attributes of successful PPP**

#### **6.1.3.1 “*What are the key attributes of successful partnerships?*”**

Respondents noted that international examples cannot be replicated directly into the local conditions, because of differences in housing markets, policy context, but these can be used to identify potential opportunities and stimulate thinking in new directions. The Table below presents the summary of the key partnership models with the stakeholders.

**Table 6.8: Key attributes of successful partnership models**

<b>Rank</b>	<b>Attributes</b>	<b>Total Counts</b>	<b>%</b>
1	Ongoing capital subsidies	8	53%
2	Access to finance at reduced cost - in the form of grants, loans below market rates or deferred interest on loans	8	53%
3	Access to land or property at reduced cost, - including discounted market price, or land made available at nil cost	7	47%
4	Mixed development to allow for cross subsidisation	7	47%
5	Security and guarantees for rentals	6	40%
6	Efficient partnership process that is not too complex	6	40%
7	A tenant mix that maximises rental revenue while achieving the organization's social mission;	5	33%
8	A rent policy that achieves an average return based rent to the extent possible while maintaining affordability for tenants;	4	27%
9	Leveraging private finance	3	20%
10	State's role to only facilitate but not as an implementing partner	3	20%
11	Optimal funding mix that makes social housing viable	2	13%
12	Pursuing a limited range of activities that achieve profits	2	13%
13	Optimal sized projects that justify the use of PPP	2	13%

## **6.2 Significance of this study**

Based on the high frequency of counts in the above Tables, these results can be considered significant to this study, as the factors were common amongst all four stakeholders.

## **6.3 Validity and reliability**

Validity and reliability in this research was achieved through a level of consistency and a process of standardisation in the data analysis methodology. The validity of the research was high as the findings of the research accurately represented what really happened in the context of the industry being investigated.

## **6.4 Conclusion and findings**

In Chapter 6, the research findings are analysed and discussed in more detail.



## **7 CHAPTER 7: DISCUSSION OF RESULTS**

### **7.1 Introduction**

This chapter analyses the research data presented in Chapter 6 in more detail and explores the emerging perceptions held by the stakeholders. The discussion was guided by empirical data gathered and frequently taps into the insights from the secondary data discussed in Chapter 2 and 3. The findings were drawn from the careful analysis and interpretation of data.

### **7.2 Research Question 1: The challenges limiting growth of the sector**

This question sought to identify the challenges in social housing delivery. Whilst the responses may not be regarded as entirely conclusive in terms of all the challenges experienced in social housing delivery, the responses indicated aspects that the respondents considered significant to the growth of the sector and their involvement in this sector.

#### **7.2.1 Financial Constraints**

Studies in social housing have highlighted that financial constraints are a key impediment to the growth of the sector (SHP: SPSH Diagnostic review).

Across the four sample groups, stakeholders considered the main challenge in social housing delivery to be the business model. Social housing, by its nature, aims to provide affordable accommodation to low to middle income households who otherwise cannot afford private sector (market linked) accommodation. The capacity of the sector to generate surpluses and invest in growth is inevitably limited by its core social objective. This social mission, by its very nature, generates lower rental revenue and can involve higher operational costs (i.e. the conflict between developmental objectives and profits). Most respondents recognise that this task warrants some form of government support. However, it is the nature and extent of that support that is a challenge and key to the functioning of the social housing system.

#### **7.2.1.1 Funding gap**

When social housing was conceptualised in the early years, government's support for social housing was manifested in the form of an institutional subsidy disbursed to institutions providing accommodation to the subsidy target market comprising of households with income of less than R3500 a month. The institutional subsidy was intended to contribute towards developmental costs of units. These included construction costs, the cost of land or cost of property in the case of refurbishments and conversions. These costs have escalated to an all time high in the last few years while the value of the subsidy, at R41 000, has not changed much since then. The quantum of the institutional subsidy is,

therefore, widely regarded as inadequate, suggesting a funding gap between developmental costs and the available funding.

These findings are in line with studies conducted by Eighty20 for the Social Housing Foundation, (2008) into the social housing market.

#### **7.2.1.2 Access to subsidies**

Another shortcoming of the subsidy mechanism highlighted by interviewees were the challenges experienced in accessing subsidy finance. Interviewees were concerned about the lengthy and bureaucratic process required to obtain subsidies. They also highlighted that there are considerable and the subsequent significant delays in receiving the funds once approved.

#### **7.2.1.3 Public budgetary constraint**

When the new social housing policy (SHP) was introduced in 2008, a restructuring capital grant (RCG) was introduced to address the shortcomings of the institutional subsidy (SHF, 2006). The market for social housing was expanded to include households with incomes between R1500 to R7500 per month. According to the revised social housing policy the value of the subsidy available to projects in identified restructuring zones varies, depending on the mix of units, starting at R120 000 per unit and this was considered adequate to address the shortfalls of the institutional subsidy. However, interviewees raised concerns about the limited number of projects that could be funded with the low

amount of budgeted restructuring capital grants available per annum. Therefore, this budgetary constraint has been cited as a severe limitation to growth of the sector. Rust, (2006) also highlighted that many practitioners have selected to forego the subsidies.

#### **7.2.1.4 *The high cost and access to debt funding***

The high cost and access to debt funding is a challenge to growth that was cited by the majority of the respondents. To fill the funding gap mentioned above, institutions are required to raise funds from other sources. The larger institutions have relied heavily on their surpluses and their strong balance sheets to raise debt funding with little or no grant funding. The smaller institutions that have little or no organisational equity and weak balance sheets have struggled to afford debt funding. The inadequate capitalisation and reliance on expensive debt has thus contributed largely to the SHI inability to deliver on a large scale.

#### **7.2.1.5 *Availability and cost of land and buildings***

Institutions highlighted that, in the past, social housing developmental costs were significantly reduced by the availability of cheap land and/or free land disbursed to SHI by municipalities. Recently, institutions do not receive free land and have had to compete with the private sector for available, well located land at market set rates. The reasons given, according to institutions interviewed, are that the public finance management act (PFMA) and the municipality finance management act (MFMA) does not allow disbursement of

land to private entities. This has put financial pressures on the ability of the SHI to develop projects.

#### **7.2.1.6 *The expensive basic services delivered by local municipalities***

Interviewees also indicated that the inefficient and expensive basic services delivered by local municipalities increase the operating costs of institutions, as most of them have to augment these services by hiring private security firms. Furthermore, it was the view of most practitioners that these expensive services delivered by municipalities exacerbate the affordability constraints in the low income market.

This concurs with findings of a study by McCarthy for the Social Housing Foundation (McCarthy, 2009), that analysed the impact of municipal charges on rental and affordability levels. The study showed that in Johannesburg, Cape Town and Ethekewini there were a range of factors resulting in inequities in the application of municipal and utility charges between lower income households living in formal rental stock and households in ownership schemes. Overall, the study found that municipal charges had an impact on the affordability of better located rental stock to low income and lower middle income households and affecting the potential for private landlords to develop affordable rental stock.

### 7.2.2 Capacity constraints

Over and above these factors mentioned above, a crucial key constraint to the growth of social housing in South Africa was the limited organisational lack of capacity of social housing institutions (SHI). Introduced just over a decade ago, social housing is a relatively new niche in South Africa. The social housing institutions have not yet provided the significant impetus expected of them when they were initially set up. Although experience has been gained in this sector over the years, experience is still limited. Interviewees cited that only a few institutions (five institutions were frequently mentioned) were considered to be highly capacitated. The lack of capacity relates to lack of project management skills, property management skills, management and weak governance. Practitioners also observed that SHI are developmental oriented more than business oriented, a view highlighted by one respondent: *“The SHI attract activists rather than commercial astute people.”*

Furthermore, the institutions do not remunerate well and, therefore, cannot attract the right skilled people because of funding constraints. A lack of suitable governance and management capacity has been evident within some of the SHI.

This concurs with the diagnostic review by SPSH. The revised social housing policy (2008) also recognises the lack of capacity in this sector has led to the disappointing delivery rate by institutions.

### **7.2.3 Legislative and regulatory environment**

Participants identified a changing policy landscape as a barrier to growth because it constrained their ability to plan. A large number of respondents viewed the rental regulatory framework as a significant barrier in the growth of the sector. The concerns relate to the management and the process of evictions, which are perceived to be highly inefficient and expensive in the context of rental laws that criminalises evictions without a court order. They suggested that a rental regulation that balances the tenant's rights with those of property owner's is necessary to functioning of the rental markets. This was also cited revised Social Housing Policy as an area to address.

### **7.2.4 Summary**

Whilst SHI have made some grounds in this sector, their capacity to deliver is limited by the factors identified in this section. The capacity building initiatives suggested by researchers and the SHP have thus far not had an impact. It is clear that the social housing sector is still underdeveloped, as noted by recent research in this sector (Sigodi, *et al.*, 2002). Within the current context, scale is thus hard to achieve in the sector given the limited capacity and experience, and the unsupportive environment.

The empirical phase of the research also reinforced a consensus across government, the private sector and social housing experts that providing

housing to low income people is inherently a social good that is government's responsibility. Most parties, therefore, recognise that in the short to medium term, this warrants government support. It is, however, the nature and extent of the government support required for efficient functioning of the social housing market that is less clear.

Given the current budgetary and capacity constraints in the sector, it is also recognised that the national government cannot, on its own, supply the housing needs of the country and thus need to attract housing investments from sources outside the state. It is the nature of these relationships (PPP) and the interventions (SHI) that would balance the social and commercial objectives that are challenging.

The next section explores the suitability of PPP within this context.

### **7.3 Research question 2: The suitability of PPP in social housing**

This section presents findings on the respondents' perceptions regarding the appropriateness and effectiveness of PPP in delivering large scale social housing, the benefits and practical issues with PPP, the critical success factors for PPP, and the approaches that can be used to stimulate social housing PPP. These findings are linked to the theory in Chapter 3.



Given the challenges identified in the social housing sector, respondents were asked whether they thought that public private partnerships (PPP) were a suitable intervention to facilitate increased delivery of social housing.

Most of the respondents agreed that PPP were, in general, one means of achieving scale in this sector. However, according the majority of the respondents interviewed (88%); the pure form of a PPP as regulated by the National Treasury was not the most suitable partnership model for social housing.

### **7.3.1 The benefits of PPP**

The respondents highlighted that the main benefits that could be obtained from properly, structured partnerships between the public, the private for profit and not for profit sectors, were the synergies that could be achieved from pooling of resources. These included both financial and management expertise, the sharing of risks, financial benefits, and the high quality of services delivered through PPP. Unlocking these resources would ultimately enhance the sector's ability to deliver at a larger scale.

The following is a discussion of the benefits raised by respondents with PPP as illustrated in Table 6.3.

### **7.3.1.1 *Financial resources and appropriate financial analysis***

The international literature on this issue indicates that in most western European countries finance, or the lack thereof, is the key impetus behind the drive for increasing private sector involvement in the social housing sector. As public funding has been cut back, social landlords have been forced to look for other sources of finance for regeneration projects (Scanlon and Whitehead, 2007).

Given the financial constraints identified by the stakeholders as limiting growth of the South African social housing sector, PPP are regarded as one way to unlock private finance and achieve the optimal blend of funding required to make social housing work. Respondents highlighted that the rigour and due diligence involved in PPP provided value for money. This benefit has been demonstrated in several studies (Akintoye *et al* (2003); Norwood and Mansfield, 1999; Huang and Chou, 2006; Saunders, 1998).

PPP subjects capital expenditure decisions to the ruthless scrutiny of private sector commercial practices. Furthermore, the public sector partner is able to cap its final service costs at pre-determined levels through the concessional agreement made with its private sector counterpart (Tiong & Anderson, 2003). The PPP should be less expensive for the public sector than traditional procurement. It is thought that, since PPP approaches encourage private sector

commercial efficiency to replace public sector bureaucratic inefficiency, it is reasonable to expect that total project cost can be reduced.

### **7.3.1.2 *Efficient execution and management***

The interviewed stakeholders indicated that PPP hold the promise of efficient execution and implementation of the development process of social housing, given the capacity constraints evident in this sector. Partnerships will deliver improved project management, cost, time and operating efficiency of the end-result (whole of life costing) by transparent accountability procedures.

This concurs with literature, which demonstrates that partnering can also raise effectiveness in the development process in that it leads to the pooling of expertise, resources, and skills in a collaborative fashion rather than a purely competitive one, bringing together the strengths of diverse backgrounds for the public good (Mackintosh, 1992: 210; Haughton & Whitney, 1989: 9).

### **7.3.1.3 *High quality of services***

Respondents also pointed out the financial benefits of partnerships, by providing high quality services at a lower cost. This is supported by the literature, which argues that PPP have greater potential in delivering high-quality services at lower costs than those available through public investment and government provision of the same services (Moszoro & Gąsiorowski, 2008;

Hemming, 2006). The higher quality is achieved by bringing together the strengths from both the public and private sectors (Hemming, 2006).

#### **7.3.1.4 Risk sharing**

One of the main advantages of the PPP approach mentioned by respondents was that the public sector and private sector can share risks at different stages, and risks would be allocated to the party who is able to best manage it.

These studies show that partnerships achieve better value for money because it becomes possible to allocate particular risk to the partner best able to manage that risk (e.g. Grimsey & Lewis, 2002; Li *et al.*, 2005a; Shen *et al.*, 2006).

#### **7.3.1.5 Ownership and management synergies**

Since affordable rental housing investments provide a lower financial return with the same cost of production as 'non-affordable' rental housing therefore, the private sector will not be keen to invest in this sector without the partnership of government. On the other hand, the government may leverage their budget by using partnership arrangements to provide more housing outcomes. Stakeholders believed that the parties needed to work together to determine the best comprehensive outcome for social housing, stressing that a mutual beneficial model would be crucial to the success of any partnering arrangement.

In recent years, there has been a growing appreciation among policy makers and practitioners working in the regeneration field that the problems of target

areas are complex and demand a multi sectoral response (Coulson, 2005). Norris, M. & Redmond, D. (2009), emphasise that, the multi agency partnerships are potentially synergistic (i.e. the partners create more together than they can separately). This is because they involve the pooling of resources. Furthermore, the negotiation and co-operation involved can encourage public-sector partners to adopt a more business-like approach, while private sector partners may become more socially minded (Ball, Le Ny, & Maginn ,2003).

The non-profit entities interviewed believed that the sector would benefit and be more efficient with increased private sector involvement.

### **7.3.2 Practical issues with social housing PPP**

To the extent that most of the respondents recognised the benefits of partnerships and the significant contribution they can make to social housing delivery, given the inadequate rate of delivery in social housing, the majority indicated that PPP are very complex. The following is a discussion of the challenges raised by respondents with PPP as shown in Table 6.5.

#### **7.3.2.1 Complex structures**

The finance structures to obtain the optimal funding model can be very complex and time consuming. *These complex structures can lead to accounting*

*problems at a later stage. However, it is these structures that make the partnership work (Respondent)*

Furthermore, social housing PPP include additional complexity such as tenant participation and community building which is “*difficult to quantify in a financial spreadsheet*”. (Respondent)

This is supported by Deloitte’s research, which mentions that the ongoing involvement with tenants is a challenge in social housing PPP. Private-sector bidders for social housing PPP projects are often presented with a situation where the financial rewards are less and the operational demands are more complex than for other infrastructure PPP projects (Deloitte Research, 2006).

#### **7.3.2.2 High transaction costs**

The complex financial structures can result in protracted negotiations with associated costs (e.g. legal costs etc.). Due to the high transactional costs of PPP, for smaller projects, traditional PPP processes (i.e. the National Treasury process) can be particularly costly when weighed against the perceived project’s modest revenue streams. This high cost can deter possible private partners from bidding if they feel future revenue is unlikely to outweigh transaction costs.

### **7.3.2.3 Bureaucratic treasury guidelines and process**

The National Treasury's PPP guidelines and processes were particularly regarded as too bureaucratic and the time it took to receive feedback in each step was long. PPP regulations require formal National Treasury authorisation of any national and provincial PPP in various steps. The first step authorisation is based on a completed option analysis/feasibility study. There are three evaluation criteria: affordability (budget impact); value for money; and transfer of appropriate technical, operational and financial risk.

Parties felt the same benefits could be achieved without the bureaucracy, and a faster, "loose PPP" would be more appropriate, "*where parties sat in the same table to negotiate.*" (Respondent)

### **7.3.3 Constraints to the formation of social housing PPP**

This section discusses stakeholder's perception about the constraints to the formation of social housing PPP in South Africa. Respondents identified the following factors as constraints as illustrated in (Table 6.6):

#### **7.3.3.1 *Conflicting interests between the parties (commercial vs. social focus)***

Each party wants to minimise risk and maximise return on its investment. The private sector requires reasonable financial return from its investment and the government wants to tightly control affordable housing development to maintain

maximum social benefits. The contradiction between investment decision-making criteria of government and the private sector has impeded the implementation of partnerships.

### **7.3.3.2 Public sector's perceptions about the “for profit” entities**

Parties in a social housing PPP have to work across boundaries to be able to coordinate and to optimise the resources and to maximise affordable social housing outcomes. Respondents highlighted that collaboration and innovation in this sector has been constrained by the perceptions the public sector has about “for profit” entities (i.e. that they are “evil” and only want to maximise profit at the expense of the poor). Evidence, on the other hand, shows that there are “for profit” entities that are reaching the downmarket in the inner city without government’s support (Madulamoho, AFHCO etc.) and would do more with the necessary support.

### **7.3.3.3 Trade-off between financial and Social Objectives**

To be viable, a PPP project must be financially attractive to the private sector. However, the sector is perceived as offering no returns and very risk in relation to other sectors. From a funding perspective, this has hampered the creation of PPP.

Interviewees highlighted that the main constraint to partnerships is the perceptions of the sector as an unfavourable investment choice for the private



sector because it is not offering a fair return on investment. The main challenge cited was to find an optimal business model that balances the social objectives of government with the commercial focus of the private sector.

The role of the private sector in funding low income households was questioned, as it was believed that low income sector should be left to government, as it was the government's role to provide shelter to low income households

*“Government should not be competing with the private sector, but provide shelter to markets that are not catered for by the private sector” – Respondent*

*“The private sector has shareholders. It is the responsibility of the government to provide social housing.” Respondent*

However, the Brickfields experience has also demonstrated that the private sector can generate returns from social housing project:....*“until about two years ago there was no interest from commercial banks. Attracting private finance was limited by the negative perceptions of high risks with little or no returns. Our experience has shown that this is not the case, as the sector can be very profitable when structured well. We have now seen some for more developments of this kind following the success of the Brickfields project”.*  
(Respondent)

#### **7.3.3.4 *Insufficient incentives***

The basic cost of construction is similar across the board but the primary factors that drive up cost are land prices, cost of finance. If land was available at viable costs for the developers, then they would construct houses for the income groups. Respondents indicated that the PFMA does not allow local authorities to disburse land to private entities. The government should focus on reducing these costs.

#### **7.3.3.5 *Changing policy landscape, regulatory and legislative environment***

Respondents identified a changing policy landscape as a barrier to growth because it constrained their ability to plan for the future. International examples where growth has been facilitated through debt demonstrate that financiers require some degree of certainty in the policy framework in which social housing operates.

#### **7.3.3.6 *Lack of critical experience (Appropriate models)***

Parties in social housing felt there was the lack of critical experience with social housing PPP was a hindrance to the formation of PPP.

### **7.3.4 Critical success factors for social housing PPP**

As identified in the literature, the suitability, the extent and success of the use of PPP depends on, amongst other things the market and environment, the economic strength and prevalent political environment of a particular country. The adoption of PPP also requires a functioning market and an enabling institutional environment. This section presents findings on what the respondents' believed were the critical success factors to PPP in social housing, as illustrated in Table 6.7.

The following issues were highlighted as key to the successful delivery of social housing PPP projects:

#### **7.3.4.1 *Balance between social and commercial focus***

The study also suggests that a balance between the investment objectives of each party should be considered.

#### **7.3.4.2 *Financial support***

The lack of funding was seen as the major impediment to the formation of social housing PPP. PPP would, therefore, depend on the government making available sufficient grants and subsidies for social housing in the short to medium term.

#### **7.3.4.3 *Creating a favourable investment environment***

The willingness of private investors to participate in social housing PPP projects depends greatly on the environment in which these projects are operated. Therefore, for PPP to work, and in order to increase the attractiveness of social housing PPP projects to private investors, government may need to provide project specific assistances and/or guarantees, such as the guaranteed minimum revenue and tax reduction for a certain period. State support and incentives are indicated as key factors for success in social PPP projects.

#### **7.3.4.4 *Establishing adequate legislative and regulatory framework***

The introduction of private finance into social housing requires a certain regulatory environment that will not change with a whim. It has been emphasised that the establishment of a sound regulation framework is a prerequisite for PPP. A well-structured regulatory framework cannot only increase the willingness of the private sector to participate in social housing development, but also increase benefits to the government by ensuring that the projects operate efficiently. Such a framework is needed to secure proper risk allocation and avoid potential corruption in the PPP implementation process. However, over regulation that may be a burden and frustrate PPP, should also be avoided.

Lenders want to lend to reputable institutions. The role of the SHRA to accredit and monitor performance of SHI is seen as significant. Extensive support from

the state and legislative, regulatory and administrative authorities, together with financial support, is essential.

#### **7.3.4.5 *Political commitment and stability***

Political stability was also highlighted as a key, success factor to PPP. An unsettled political and economic environment would complicate the pursuit of goals and objectives (i.e. a long term view). Uncertain political and perceived potential political interference will be a hindrance to the formation of the PPP. Housing is an important political and social issue in South Africa. The respondents are not convinced of the ability of government to let it go and let the market run it. Coupled with that is the change in government can often come with a change in direction in policy. This illustrates the importance of stability in the policy and strategy. Uncertain or often changing policy results in uncertainty and raises interest rates. Under these conditions, the housing finance system, is less able to mobilise adequate resources or make long term investment.

#### **7.3.4.6 *Macro economic environment***

The vulnerability of the low income market and labour force to economic conditions is a challenge in this sector. The global economic recession exacerbates the difficulties of delivering affordable social, raising challenges with regards to future developments. Inflation is putting real disposable income under pressure. At the same time, the cost of land, property, and construction

has escalated. This illustrates the importance of stability in the macroeconomic system. This also emphasizes the need for government to increase its subsidy system so as to match the cost escalations.

#### **7.3.4.7 Market appetite**

This implies that the project should create a genuine business opportunity that is likely to attract a sufficient number of private parties and create an effective and competitive bidding process. PPP also require a project to be viable to ensure that the project will be financially secure and that the private sector can make a reasonable profit to cover their project expenditure. In general, there is considerable market appetite for PPP deals in South Africa. However, according to industry practitioners, deal flow has been tortuously slow in the South African PPP market. When the Job Summit Project was presented to the private sector, there was interest from the private sector. Respondents believed that commercial banks were showing interests in social housing PPP.

#### **7.3.4.8 Institutional factors**

A mature institutional environment was highlighted as critical to the success of social housing PPP. According to the Deloitte Research, 2006, South Africa's PPP market is still at the first stage of development: designing the partnership policy and legislative framework, getting the procurements and contracts right and building the marketplace by encouraging the private sector to bid on these kinds of contracts. The market is well developed and has been active for eight

years with past projects including toll roads, hospitals, prisons, office accommodation and power generators.

Such an institutional environment could be composed of several components, discussed below:

- First, the presence of explicit PPP legislation or at least a policy towards PPP would provide great confidence to the public and private sectors to enter into a PPP transaction by laying out the rules of engagement
- These arrangements could further be enhanced through the use of standard, model concession agreements specifically for social housing, where the risks and their allocation are well-known beforehand.

#### **7.3.4.9 Flexibility**

PPP need institutions that are pragmatic and less rigid to come up with innovative models. One respondent cited that *“you cannot expect to cut and paste what works in high end markets into social housing*

#### **7.3.4.10 Understanding of the sector**

An understanding of the social housing market and flexibility is required to be able to find win-win, optimal models that work within allowable risks. Respondent noted that some of the negative perceptions about the sector stem

from a lack of awareness and knowledge about the developments in this sector. A clear understanding of the challenges faced in this sector was therefore crucial for success of any PPP arrangement.

#### **7.3.4.11 *Environmental factors***

The PPP approach requires strong political commitment and legislative support. The existence of political willingness to enter into an arrangement with the private sector, as well as the local community's willingness to be involved in a project and pay for a service, are key environmental factors that determine whether or not PPP will survive in the long term.

#### **7.3.5 Approaches to stimulate social housing PPP**

Given the identified success factors for social housing PPP, the respondents identified the following recommendations for government to stimulate partnerships:

The first recommendation was that government should make more funds available for social housing. This will increase investor confidence in this market.

Government should facilitate and create an enabling environment to stimulate investment in the social housing sector by-



- Providing investor incentives such as cash back rebates, tax for developers, and other incentives to lower the cost burden for tenants such as rental guarantees and utility subsidies
- Providing a stable regulatory and legislation framework
- The primary factors that drive up costs are land prices and the cost of finance. Government should focus on reducing these costs by making available discounted land and property for development. If land was available at viable costs for the developers, then they would construct houses for the low to middle income groups.

### **7.3.6 Summary**

This section looked at the suitability of PPP in the social housing sector. Stakeholder's were against a formal PPP as regulated by the National Treasury, but indicated that partnerships would be effective to provide comprehensive solutions to the housing challenges. The benefits of partnering are the resources and expertise that each party brings to the table in the following areas: finance, land and property, production and development and professional expertise.

## **7.4 Research Question 3: Key attributes of successful PPP models**

### **7.4.1 Introduction**

South Africa can gain valuable insights from studying international experience in social housing PPP. Chapter 2 demonstrated that a variety of partnership models for increasing the supply of social housing were possible. Key components of successful partnership models applied in the two countries studied, were identified in Chapter 2. These components were used as a discussion point in the interviews conducted for this study. This section discusses the components that the stakeholders regarded as most appropriate to the local context.

### **7.4.2 Key components of partnership model**

Stakeholders indicated their keenness to find mutually beneficial solutions in the social housing sector. Respondents highlighted a few components that would or would not work, and also suggested a few from their experience in this sector. These were the potential to subsidies utilities and provide rental guarantees.

The key component highlighted by respondents was the crucial role the land availability of cheap or free land plays in the viability of social housing projects.

The stakeholders believed that the following components would be appropriate as building blocks for social housing partnerships in South Africa:

**Table 7.1: Key components of PPP model**

Barrier	Description	Strategy	Assessment in South Africa
<b>Inadequate revenue base</b>	<b>Income based rent policies for some social housing institutions do not provide sufficient income to sustain operations and thus constrain the capacity of organisations to sustain debt financing for growth.</b>	A rent policy that achieves an average return based rent to the extent possible while maintaining affordability for tenants;	This is identified by the Social Housing foundation. However, rent setting is left up to the SHIs
		A tenant mix that maximises rental revenue while achieving the organisation's social mission;	The Social Housing Policy identifies this as crucial to sector viability. There were however concerns about social housing competing and crowding out the private sector.
		Pursuing a limited range of activities that achieve profits;	For example, retail space can be provided on the ground floor of the developments where the additional revenue streams can subsidise low income rentals. The respondents felt this was easier to be achieved with new build projects. They also cautioned against SHI venturing into areas that they have no expertise in.
<b>Limited organisational capacity of some SHIs and economies of scale</b>	<b>A portfolio under management of 2000 units to break even</b>	Optimal sized projects that justify the use of PPP. (Bundling and multi-phased approach);	Transaction costs in PPPs are high for smaller projects. This however would be a challenge in the context of availability of land in the suitable areas.
<b>The funding gap</b>	<b>There is a gap between available subsidies and the actual development</b>	Access to land or property at reduced cost, - including discounted market price, or land made available at nil cost	The Housing Development Agency was set up to unlock government land for housing developments. However, respondents expressed concern over the delays with unlocking government land.



	<b>cost.</b>	Sufficient and stable recurrent and/or capital funding support from government	Budgetary constraints and inefficient public sector processes
<b>High cost of debt funding</b>		Lower the cost of finance.  Access to finance at reduced cost - in the form of grants, loans below market rates or deferred interest on loans	The state development institutions (NHFC, GPF, NURCHA) have not delivered the impetus that they were setup for.
		government guarantees	Not currently available
<b>Insufficient equity base to facilitate leveraging debt against assets</b>	<b>The core barrier to growth was the lack of a sufficient equity base, in the form of title on properties, to enable providers to leverage debt against their assets.</b>	Transfer government owned and managed properties to SHIs at reduced costs	Stakeholders were also concerned about the government's direct involvement in property management
<b>Lack of consistent policy backing and a regulatory framework</b>	<b>A changing policy landscape is a barrier to growth because it constrains the ability to plan.</b>	Consistent policy. International examples where growth has been facilitated through debt demonstrate that financiers require some degree of certainty in the policy framework in which social housing operates.	

## 7.5 Conclusion

This section analysed and discussed the findings from the empirical phase of the research, comparing it to the secondary data conducted for this study. The findings correlated with the literature.

The next section presents the findings of this study with recommendations for future research.

## 8 CHAPTER 8: RESEARCH CONCLUSION

### 8.1 Introduction

This chapter reflects on the main research problem as outlined in Chapter 1, as well as the associated research objectives. This chapter makes recommendations to the stakeholders of this research, based on the findings and finally make recommendations for future research.

The main research objectives for this study were:

- To investigate, through literature reviews and stakeholders' perceptions, whether public private partnerships (PPP) are an appropriate and effective vehicle for increased delivery of quality and sustainable social housing in South Africa
- To identify key components of successful PPP models applied internationally that would be used as building blocks for a South African partnership.

The extent to which the research problem has been addressed is determined by the extent to which the research questions in Chapter 4 have been answered. The results from the various phases of research have been presented in Chapter 2 and 3 (non-empirical findings), Chapter 6 (empirical findings) and Chapter 7 (empirical data analysis).

### 8.1.1 Research Question 1 Findings

The first research question aimed to understand the current challenges limiting growth in the sector. Whilst headway has been made in this sector, the empirical and non-empirical analysis found that financial and capacity constraints including an unsupportive policy and regulatory environment have been the main impediments to growth in this sector. The social housing sector, as suggested by researchers (Sigodi *et al.*, 2002), is still underdeveloped, and social housing investment has been considered by industry practitioners as a risky business in comparison to other private residential and commercial investment.

The main deterrents of private sector investment in social housing projects have been the business model, as the ability to increase rentals is constrained by the affordability in the targeted income band. The capacity of the sector to generate surpluses and invest in growth is inevitably limited by its core social objective, which is to provide housing to low income households, as this generates lower rental revenue and can involve higher operational costs.

The housing policy and regulatory environment has also contributed to the inadequate delivery rate of agents in the sector. Within the current context, scale is thus hard to achieve.

### 8.1.2 Research Question 2 Findings

This research question served to assess the suitability of PPP to meet the targets of social housing by identifying the benefits, complexities and critical success factors of PPP in social housing, based on non-empirical data (Chapter 2) and empirical findings in Chapter 5.

In recent years, there has been a growing appreciation among policy makers and practitioners that the challenges of providing accommodation to low income households are complex and demand a multi-sectoral response, which could include a role for the private sector (Coulson, 2005). These multi-sectoral partnerships are envisaged as potentially synergistic, (i.e. the partners create more together than they can separately), with efficiency gains from parties pooling resources (financial, expertise and skills) resulting in efficient execution and implementation of social housing developments. Another main attraction of PPP is the sharing of risks.

Given the financial and capacity constraints that have impeded large-scale delivery (growth) in the social housing sector, this study found that PPP have the potential to increase the scale of delivery in this sector by bringing in private finance sector funding to supplement the limited public finances.

International experience and the empirical findings from this study, demonstrate that the PPP model is particularly appropriate for the delivery of mixed income developments, which includes a tenant mix (social and private housing) that



maximizes rental revenue, where a balance between the social and profit objectives of the different parties exists .

However, PPP are the most complex of all procurement options and could involve high transaction costs, especially for small projects. In this regard, it is the finding of the study that “traditional” PPP processes (i.e. the South African National Treasury process) are not perceived to be suitable in the social housing context, as they can be particularly costly when weighed against the perceived project’s modest revenue streams. The potential high cost can deter private partners from bidding if they perceive future revenue as unlikely to outweigh transaction costs. Furthermore, the feedback loop in the process is perceived to be too long.

This research also highlights some limitations to the potential for private sector involvement in social housing. Industry practitioners consider social housing investment, risky in comparison to other private residential and commercial investments. In this regard, the crucial deterrent of PPP success in social housing contexts is the country’s economic regulatory, political, and housing market contexts. The target market is vulnerable to changes in the economy, requiring a stable macroeconomic environment. PPP also require long-term investment (funding), therefore, investors need to be certain that the political and policy environment will be stable.

This study, therefore, reinforces the (belief) that in the short to medium term, whilst capacity is being built in this sector, the task of providing accommodation to the downmarket warrants government support. This study suggests investor incentives, continuing and guaranteed government financial support and a stable policy and regulatory environment are crucial to the formation of PPP in social housing.

### **8.1.3 Research Question 3 Findings**

The third research question aimed to identify key components that would be used as building blocks for future partnerships in the South African social housing sector. The empirical study in Chapter 3 and non-empirical findings, the following attributes of a partnership model were identified:

Attributes
Ongoing capital subsidies
Access to finance at reduced cost - in the form of grants, loans below market rates or deferred interest on loans
Access to land or property at reduced cost, - including discounted market price, or land made available at nil cost
Mixed development to allow for cross subsidisation
Security and guarantees for rentals
Efficient partnership process that is not too complex
A tenant mix that maximises rental revenue while achieving the organization's social mission;
A rent policy that achieves an average return based rent to the extent possible while maintaining affordability for tenants;
Leveraging private finance
State's role to only facilitate but not as an implementing partner
Optimal funding mix that makes social housing viable
Pursuing a limited range of activities that achieve profits
Optimal sized projects that justify the use of PPP

## 8.2 Recommendations and policy Implications

This section draws upon what has been learnt about social housing, in general; public private partnerships as a concept; and about social housing PPP to provide some reflective recommendations and proposals to achieve growth and

sustainability in this sector based on the findings of this report. These recommendations have not been evaluated using any formal schema, but have been guided in a loose way by principles of efficiency, effectiveness, and social inclusion. They are intended to stimulate thought and provoke discussion, without claiming to be in any way comprehensive or definitive. The recommendations are intended to guide social housing practitioners in the creation of a policy climate that works to expand the role of the private sector and to foster the formation of mutual beneficial multi-stakeholder partnerships in the area of social housing:

- This report proposes that government should consider a guarantee fund for rentals as a policy lever to reduce the cost of debt funding for social housing developments. This fund has been instrumental in unlocking private finance internationally
- Government should also consider a transfer of all government managed social housing units to the private, not for profit, sector at reduced rates. This will build their asset base and enhance the ability to leverage debt finance. It is the view of the author that government's role should be to facilitate and stimulate investment by creating an enabling environment. This suggests that government cannot be a direct provider of property and compete with the private sector

- Further investment in the sector can be stimulated by introducing comprehensive incentives directed at investors and to the tenants. These include tax breaks, cash rebates for investors, and utilities and rental subsidies
- It is the opinion of the author that the private sector is keen to make a significant contribution in the social housing market, provided there are fair returns to be made. Investor confidence will depend on government's commitment, and support. The main support that government can make is to ensure availability of subsidies and improve its planning capabilities.

### **8.3 Limitations and recommendations for future research**

This research had the following limitations:

- There was limited data available on the availability of rented accommodation, relating to privately owned and managed dwellings, state owned and managed dwellings, and social housing dwellings. The data used in this study was obtained from other previous studies in the rented accommodation
- This study is also limited in the sample size. A larger sample size would ensure that the results could be better generalized by including other developers, contractors, project financiers and other stakeholders involved

- This study could be considered as the first step to understand the viability of PPP in social housing procurement projects. A robust financial model would add weight to the research. Further studies towards the development of a financial model which would analyse the options for the housing sector and identify revenues and costs, capital and recurrent funding requirements, funding shortfalls, the optimal levels and costs of debt, and capacity for growth is recommended. This modelling could be based on the cash flow analysis of a small number of indicative social housing providers and also enable sensitivity analysis of key variables
- During the empirical phase of the research, there were many positive reviews of the Brickfields PPP projects. A case study of the Brickfields project would be beneficial for the sector to assess its appropriateness as a model for future partnership
- An analysis of the options for expanding and maturing the social housing sector, including assessment of tangible and intangible costs and benefits is recommended for future study
- It would also be beneficial to study the appropriateness of PPP to address other housing challenges such as the affordable ownership sector
- Further research to understand the demand and supply dynamics of rental housing is recommended.

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## APPENDIX A: LIST OF RESPONDENTS

ORGANISATION	RESPONDENT	DESIGNATION	CONTACT DETAILS
Affordable Housing Company (AFHCO)	Renney Plitt	Managing Director	+27 11 221 8300
Trafalgar Property and Financial Services Group	Andrew Schaefer	Managing Director	+2711 214 5200
Nedbank	Manie Annandale	Head: Affordable Housing Unit, Corporate Property Finance	+27 11 294 0261
The Banking Association of South Africa	Cas Coovadia	Managing Director	+27 11 645 6700
National Housing Finance Corporation (NHFC)	Chris Moodley	Assistant Executive	+27 11 644 9800
National Urban Restructuring Housing Agency (NURCHA)	Linda Sing	Independent Non-Executive Director	+27 11 771 4000
Gauteng Partnership Fund (GPF)	Boni Muvevi	Chief Financial Officer	+27 11 290 6637
Trust for Urban Housing Finance (TUHF)	Paul Jackson	Chief Executive Officer	+27 11 276 1440
Learning Strategies	Larry Hobson	Director	+27 11 447 6206
Dan Smit Development Capacity	Dan Smit	Owner	+27 84 467 7211
SHI aka Management Services	Mathew Nell	Founder & Director	+27 11 447 6388
Johannesburg Housing Company (JHC)	Elize Stroebe	Chief Executive Officer	+27 11 241 6900
Yeast City Housing	Dandy Matamela	Managing Director	+27 12 320 7962



Social Housing Foundation (SHF)	Brian Moholo	Managing Director	+27 11 274 6200
National Treasury	Kogan Pillay	Head PPP Unit	+27 12 315 5363

## APPENDIX B: MAPPING RESEARCH QUESTIONS WITH OBJECTIVES

Research Questions	Interview Questions	Objectives		
		Evaluate the extent to which practitioners believe PPP may succeed in increasing the supply of quality and sustainable social housing stock Interviews	Assess the extent to which the South African context can facilitate the implementation of PPP in Social Housing Literature review, Interviews	Identify attributes of a successful models for implementation in South Africa  Literature review, Interviews
<b>Research Question 1</b>	What are the challenges in social Housing delivery?		x	
<b>Research Question 2</b>	What are the benefits of a PPP in social housing?	x		
	What are the challenges with social housing PPP?	x		
	What are the constraints to social housing PPP?	x		
	What are the critical success factors for Social Housing PPP?		x	
	Do the South African conditions facilitate implementation of PPP in Social Housing?		x	
	What approaches can be utilised to encourage participation and to stimulate Public Private Partnerships in this sector?			
<b>Research Question 3</b>	What are the key essential components of a social housing partnership that would encourage effective delivery of social housing?			x

## APPENDIX C: SEMI-STRUCTURED INTERVIEW GUIDE

### MBA DISSERTATION - CONSENT FORM

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#### INTRODUCTION AND BACKGROUND INFORMATION

*Title of study:* **Social Housing in South Africa: Are Public-Private Partnerships a solution?**

*Purpose of this research:* To investigate the role and suitability of Public Private Partnerships (PPP ) in meeting the social housing objectives in South Africa and to develop a PPP framework for implementation based on international best practise and key stakeholder perceptions and preferences.

#### RIGHT OF REFUSAL TO PARTICIPATE AND WITHDRAWAL

You are free to choose to participate in the study. You may also withdraw any time from the study. You may also refuse to answer some or all the questions if you don't feel comfortable with those questions.

#### CONFIDENTIALITY AND ANONYMITY

The information provided by you will remain confidential; nobody except the researcher will have access to it. Your name and identity will also not be disclosed at any time. However, the data may be seen by the Ethical review



committee and may be published in journal and elsewhere without giving your name or disclosing your identity.

### **AVAILABLE SOURCES OF INFORMATION AND RESEARCHER CONTACT DETAILS**

If you have any further questions you may contact the:

- Research Supervisor, Ms Linda Sing at [singl@gibs.co.za](mailto:singl@gibs.co.za) or
- Researcher, Ms Yandisa Sobuza, at O82 339 9064, or mailto: [ysobuza@gmail.com](mailto:ysobuza@gmail.com)

### **CONSENT**

I have read and understand this consent form, and I volunteer to participate in this research study. I understand that I will receive a copy of this form. I voluntarily choose to participate, but I understand that my consent does not take away any legal rights in the case of negligence or other legal fault of anyone who is involved in this study.

Respondent Name: \_\_\_\_\_

Signature : \_\_\_\_\_

Date: \_\_\_\_\_

## Semi structured Interview Guide

### Research Question 1 (Sector specific challenges): Interview Question 1 to 4

- Question 1. What are the challenges in social housing delivery?
- Question 2. Is the private sector currently involved or interested in this sector?
- Question 3. What are the limiting factors for private sector involvement?
- Question 4. Are the current incentives sufficient to attract public sector involvement?

### Research Question 2 (PPP in social housing): Interview Questions 5 to 10

- Question 5. In your view, are PPP an appropriate sustainable delivery mechanism for social housing?
- Question 6. What are the potential benefits of a PPP in social housing?
- Question 7. What are the negative factors that deter stakeholders from participation in social housing PPP ?
- Question 8. What are the necessary conditions for success in social housing PPP?
- Question 9. Do the South African conditions facilitate formation of PPP? If No, What are the conditions that constrain the implementation of PPP in social housing?
- Question 10. What approaches can be utilised to encourage participation, and stimulate public private partnerships in this sector?

### Research Question 3 (Optimal model attributes): Interview Question 11

- Question 11. What are the key essential components/attributes of a social housing partnership that would encourage effective delivery of social housing?

## APPENDIX D: KEY COMPONENTS OF PPP MODEL

Key Components	Purpose
Access to land or property at reduced cost, - including discounted market price, or land made available at nil cost	Lower cost of development thus extending reach
Access to finance at reduced cost - in the form of grants, loans below market rates or deferred interest on loans	Lower the cost of finance
A tenant mix that maximises rental revenue while achieving the organisation's social mission;	Maximise revenue; Cross subsidisation
A rent policy that achieves an average return based rent to the extent possible while maintaining affordability for tenants;	Maximise revenue
Optimal sized projects that justify the use of PPP. (Bundling and multi-phased approach);	Reach scale to break even (Economies of scale)
Pursuing a limited range of activities that achieve profits;	Maximise revenue; Cross subsidisation
Leveraging private finance	Favourable investment environment
Transfer government owned and managed properties to SHI at reduced rates	Increase asset base of SHI to build capacity to leverage other sources of finance