

Submission

**Submission to the
Productivity
Commission Inquiry
into First Home
Ownership**

**Australian Housing
and Urban Research Institute**

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PURPOSE OF THIS SUBMISSION

This submission reports key findings from the housing and policy research evidence base developed by the Australian Housing and Urban Research Institute (AHURI). The available research evidence, relevant to the Terms of Reference of the Inquiry, has three elements:

1. contextual changes in the housing market conditions within which first home owners are operating;
2. specific findings about the purchasing behaviour of first home owners
3. specific findings about the purchasing opportunities of potential first home buyers and the housing affordability difficulties faced by this group.

SUMMARY OF KEY POINTS

1. Demand for new housing is projected to remain high until 2011.
2. Aspirations to enter home ownership continue to be high but unrealised for many.
3. Home ownership amongst 25-44 year olds fell by 10 percentage points, 1986-96.
4. Government tax concessions to home owners are estimated to amount to \$21 billion in 2001, yet young, lower-income purchasers aged between 25 and 45 with incomes in the three lowest quintiles receive little of this assistance.
5. The purchasing behaviour of first home owners is being affected by labour market changes such as increased casual and insecure employment.
6. Whilst there is a risk of housing affordability difficulties amongst first home owners if interest rates rise significantly or if there is an unanticipated interruption to their income, many households on lower incomes (primarily private tenants in the bottom 40% of the income distribution) face such high housing costs that they are unlikely to be able to save the money required to become a first home owner. Housing affordability problems in the private rental market can translate into a home ownership accessibility problem.
7. The First Home Owners Grant is estimated to have a small positive effect on the long-run home ownership rate.
8. The Australian Government Building Write-Off Allowance and State and Territory Land Tax and Stamp Duty are ineffective in promoting the supply of private rental dwellings, particularly at the low-cost end of the market.

THE AUSTRALIAN HOUSING AND URBAN RESEARCH INSTITUTE

The Australian Housing and Urban Research Institute – AHURI – is the national policy research institute responsible for the conduct of research on housing and urban policy matters. AHURI aims to inform policy development by governments, industry and the community sector, and to stimulate debate on these issues in the broader community. Funded primarily by the Australian Government and all State and Territory Governments, the Institute comprises seven university based Research Centres located around Australia. A small management company, AHURI Limited, is responsible for the day to day management of the Institute.

Since its re-establishment in 2000, AHURI has undertaken more than 100 research projects on a wide range of housing policy matters. The findings from this research programme are available free from the AHURI website: www.ahuri.edu.au.

AHURI research projects relevant to the terms of reference of the Inquiry are listed at Appendix A.

AHURI *Research Agenda 2004* (AHURI 2003) sets out current priority policy research areas that have been identified by the Australian Government and State and Territory governments, the community and non-government sector and expert academics in relevant fields. Three key programs of research underway relate to:

- Housing Assistance and Non-Shelter Outcomes
- 21st Century Housing Careers and Australia's Housing Future
- Housing Affordability for Lower-Income Australians.

In 2004 a new suite of projects will commence addressing the following themes:

- housing assistance programmes
- housing futures
- programme integration and housing assistance
- urban management and infrastructure
- transforming communities
- indigenous housing
- homelessness and marginal housing

- the housing system.

The establishment of AHURI by Australian governments in 2000 has been important in redressing many years of under-investment in housing and urban policy research. In collaboration with its government stakeholders AHURI has concentrated development of the policy research evidence base, primarily, on issues associated with housing assistance for low-income Australians.

The Productivity Commission Inquiry into First Home Ownership has underlined the importance of the operations of the housing market at large to the Australian economy, and the nexus between housing and urban development issues. The sound questions raised by the Productivity Commission in the Issues Paper (Productivity Commission 2003) point to an opportunity for industry, universities and government to invest in an ongoing program of research that will develop the evidence base for effective policy making into the future.

RESEARCH EVIDENCE ON THE CHANGING HOUSING MARKET CONTEXT FOR FIRST HOME OWNERS

A critical issue for the Inquiry is whether the current housing market conditions for first home owners are primarily cyclical, and will adjust at some point in the near future, or whether current market conditions reflect a structural shift in the long-run market conditions.

Demographic change and its impact on housing demand is one key aspect of the housing market conditions within which first home owners are operating. In an AHURI research project, McDonald (2001a,b) has developed a sophisticated model that enables accurate projections of the demand for housing to be made. The research used 1996 Census data to project housing demand across 71 regions of Australia to 2011.

Detailed findings from this project are available from the AHURI website (McDonald 2001a,b). The key findings are as follows:

- demand for new dwellings in Australia is projected to remain high until 2011, particularly in the outer regions of the major capital cities, driven by smaller household sizes and an ageing population;
- projected housing demand across Australia is approximately 128,000 dwellings a year between 2002 and 2011. This compares to 148,000 dwellings per year in recent boom years and suggests that the housing industry will not experience a severe bust following this boom;
- social trends, such as the move towards smaller households, and the demographic reality of an ageing population, will continue to drive demand for new housing and will contribute to keeping demand high;
- almost half a million dwellings are projected to be required in the outer areas of Australia's five largest cities between 2002 and 2011, creating a potential challenge for planning authorities;
- coastal regions on the east coast, as well as Barwon in Victoria, Adelaide's hinterland and the South West and Kimberley regions of Western Australia are all projected to experience continued high growth;
- population is expected to fall in 23 regions around Australia, mainly rural areas isolated from the major cities. But housing demand is expected to fall in only six of these 23 regions.

The demand for new housing will remain high and the aspiration for this housing to be owner occupied is also likely to remain high.

In two AHURI research projects on home ownership aspirations conducted by Baum and Wulff (2003), and by Merlo and McDonald (2002), evidence was found of continuing high levels of aspiration for home ownership, but low levels of achievement of home ownership.

The detailed findings of these projects are available from the AHURI website (Baum and Wulff 2003; Merlo and McDonald 2002). The key findings are as follows:

- Australians continue to aspire to home ownership, but less than one third of those for whom buying a home was an important short-term goal were able to achieve it within three years;
- home ownership aspirations fluctuate over time with changing social, economic and demographic conditions;
- in the late 1990s nearly three quarters of renters surveyed aspired to home ownership, particularly those households with a young child or wanting another child;
- dual income households were most likely to succeed in achieving home ownership;
- socio-demographic profiles of those who aspire to home ownership, and of those that succeed and fail in achieving this, prompt consideration of the nature of the policy supports for home ownership and of who benefits from these.

Evidence of low levels of achievement of home ownership is confirmed by an AHURI research project conducted by Yates (2002) that used Census data from 1986 and 1996 to analyse trends in the home ownership rate. The research demonstrates that through the 1990s fewer younger households were entering home ownership.

Detailed findings from this project are available from the AHURI website (Yates 2002). The key findings are as follows:

- Australia's home ownership rate fell 2.2 percentage points from 68.2% to 66% between 1986 and 1996, mainly due to a decline in the percentage of home purchasers;
- for people in the 25-44 year old age group in metropolitan areas, there was a 10 percentage point fall in the rate of home purchase;
- the main reason for these declines was rising house prices rather than changes in demographic structure of the distribution of incomes;

- rising house prices since 1996 suggest that declines in the home ownership rate may have continued. The introduction of the First Home Owners Grant in July 2000 is likely to have had a positive impact on the rate of entry to home purchase (see below);
- Census data for 2001 portray little change in the overall home ownership rate since 1996;
- Inequalities arising from the labour and housing markets are compounding one another as income differences arising from the labour market and social security system between 1986 and 1996 were increasingly reflected in, and reinforced by, the tenure differences within the housing market between home purchasers, outright owners, public renters and private renters.

Home ownership rates in Australia have fallen despite continuing high levels of government support for home ownership. The First Home Owners Grant (FHOG), \$7,000 of direct financial assistance, introduced as compensation for the Goods and Services Tax in July 2000, is perhaps the best known of these. The Australian Government, however, also provides a number of important indirect subsidies to home owners. In a recent AHURI research project Yates (2003) completed an analysis of the value of indirect subsidies provided to home owners.

Detailed findings from this project are available from the AHURI website (Yates 2003). The key findings are as follows:

- home ownership in Australia is exempt from capital gains tax and other income taxes;
- the value of these indirect subsidies to owner-occupiers in 2001 was estimated to amount to \$21 billion;
- the tax concession to owner-occupiers of not taxing capital gains was estimated to be \$13 billion in 2001;
- the tax concession to owner-occupiers of not taxing imputed rent was estimated to be a net value of \$8billion;
- in comparison direct subsidies to first home buyers (First Home Owners Grant [FHOG]) amounted to \$1billion in 2001;
- high-income (\$100,000 plus) outright owners receive a total tax benefit of \$7,000 to \$9,000 per household per year;
- home purchasers in the bottom 80 per cent of the income distribution receive a total tax benefit of less than \$500 per household per year.

RESEARCH EVIDENCE ON THE PURCHASING BEHAVIOUR OF FIRST HOME OWNERS

Two recently completed research projects by AHURI provide specific findings about first home owners.

An AHURI research project by Kupke and Marano (2002) investigated how changes in the labour market, such as insecure or casual employment, are affecting the attitudes and decisions of first home buyers. The research was based on surveys in metropolitan Adelaide and three South Australian regional centres in 1999 and 2000.

Detailed findings from the research project are available from the AHURI website (Kupke and Marano 2002). The key findings are as follows:

- the majority (60%) of first time buyers - regardless of where they lived, their employment category (permanent, contract, casual or self-employed) or the year of purchase - agreed that their concerns about job security had influenced their purchase. For many households job security concerns made them deliberately more cautious in their buying - looking in a lower price range, buying a cheaper home or borrowing less;
- employment category proved to have a stronger association with home purchase price than did household income. Those in less secure jobs bought cheaper homes; having a higher income did not necessarily translate into the purchase of a more expensive home;
- most (65%) households who reported being very concerned about job security had taken out the maximum loan they were able to secure;
- most households on weekly incomes of less than \$500, or who were struggling financially, had taken out the maximum loan available to them;
- the majority of people receiving FHOG bought low-priced homes on moderate to high incomes.

The research by Kupke and Marano is about those who have managed to enter home ownership. While the issues first home owners face are important, they tell us little about those who continue to aspire to home ownership but are unable to access it. This is a policy issue of housing accessibility rather than housing affordability. The majority of households that aspire to home ownership are in the private rental sector. It is, therefore, important to consider the capacity of this group of households to save for

entry to home ownership. A key indicator of this capacity is whether such households live in affordable housing.

An AHURI research project by Berry (2002) examined the housing affordability of private tenants in the bottom two income quintiles. Households paying more than 30% of their income in rent are assessed not to be living in affordable housing because they are unlikely to have sufficient income to pay for basic household requirements such as food and transport and certain not to be able to save the deposit needed for home purchase.

Detailed findings from the research project are available from the AHURI website (Berry 2002). The key findings are as follows:

- between 1986 and 1996, the proportion of private tenants in the bottom two income quintiles paying more than 30% of their household incomes in rent rose from 64% to 73% in the six State capital cities (and Darwin);
- the number of rental households in unaffordable housing increased by 90,000 during this period, to 227,480 by 1996;
- at a sub-metropolitan level, housing affordability is declining for private renter households in the bottom two income quintiles in both inner and outer areas of Melbourne, Sydney and Adelaide (the cities analysed in detail in the study)
- in general, affordability and locational and dwelling choices declined from 1994 to 2000 throughout both Sydney and Melbourne.

Given the housing affordability difficulties present in the private rental sector for lower-income households, and the implications of this for accessibility to home ownership, it becomes important to consider what, if any, financial assistance might successfully support access to home ownership. Amongst the options is a demand-side response (such as the FHOG) to assist households to enter home ownership, and a supply side response to promote the supply of dwellings in the private rental market, provide downward pressure on rents, and thereby improve the savings capacity of households in this market segment. In an AHURI research project by Wood, Watson and Flatau (2003) both of these forms of assistance have been assessed.

'AHURI-3M' – the AHURI Housing Market Microsimulation Model has been developed to examine issues such as which tenants might be assisted into home ownership by the First Home Owners Grant, or a measure such as a shared equity scheme as proposed by the Prime Minister's Taskforce on Home Ownership, and to examine how supply in the private rental market might be promoted.

The model provides a means of assessing the quantitative impacts of housing policy measures (current and proposed) and takes into account both the demand and supply side of the housing market. The model incorporates two key elements: a theoretical framework of the decision-making processes of housing market participants, and the implementation of that framework using representative Australian survey data.

Detailed findings from this project are available from the AHURI website (Wood, Watson and Flatau 2003).

Key findings with regard to demand-side subsidies are as follows:

- the FHOG is predicted by AHURI-3M to have a small positive effect on the share of the current Australian population who will be home owners at some point in their lives;
- When the FHOG is at the \$14,000 rate (as it was in 2001) it is highly effective in relaxing the deposit constraints of many potential home buyers;
- The FHOG, at either the \$7,000 or \$14,000 rate is less effective in easing the repayment constraints associated with home ownership;
- The FHOG assists people to enter home ownership who would probably have become home owners anyway, but it enables them to make this transition at an earlier age;
- The FHOG is predicted to be of most assistance to younger, middle income single person households in white collar jobs;
- A shared equity scheme will have impacts on home ownership rates (though with a different equity outcome for the home owners) that are larger than FHOG, provided financial institutions are willing to take high equity shares;
- A shared equity scheme is more likely to be taken up by lower income households than the FHOG;
- A shared equity scheme is less likely to simply bring forward home purchase decisions;
- Government policies that promote access to homeownership have the potential to lift homeownership shares in the short run, particularly if they are targeted in such a way that they ease borrowing constraints.

Key findings with regard to supply-side subsidies are as follows:

- The supply of affordable housing in the private rental market could be increased if the Australian Government Building Write-Off Allowance were replaced by a Low

Income Housing Tax Credit, and by amendments to State and Territory Land Tax and Stamp Duty.

- Estimates from AHURI-3M find that individual investors in the private rental market face high effective tax rates at low rates of capital gain. Existing Australian Government Building Write-Off allowances have only a marginal impact upon the tax burden of landlords. Furthermore, they are not targeted to the low rent end of the private rental market and a US style Low Income Housing Tax Credit (LIHTC) is estimated to be far more effective in promoting the supply of low-rent dwellings.
- Estimates from AHURI-3M demonstrate that State and Territory Land Tax and Stamp Duty create disincentives for single property landlords who wish to add to their investments in rental housing, and thereby potentially limit the supply of dwellings in the private rental market.

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APPENDIX A

Recent and current AHURI research relevant to the Inquiry

Completed Projects

| Title | Summary |
|---|---|
| The implications of changes in the labour market for the ownership aspirations, housing opportunities and characteristics of first home buyers | <p>Concluding report surveying first home buyers who have bought in SA in the last 2 years, to determine buyer profile in terms of employment, expectations and attitudes to job security, and how this has influenced their home purchase.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=26</p> |
| Medium and long term projections of housing needs in Australia | <p>The project brings together key Australian experts in the field of household projections and econometric modelling to formulate and develop a set of projection methods and techniques suited specifically to Australian needs and resources. The project involves consultation with users about their needs and the appropriateness of the proposed methodology.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=32</p> |
| Outcomes of home ownership aspirations and their determinants | <p>Final report examining home ownership aspirations in 1997 and the extent to which they have been realised three years later.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=34</p> |
| New approaches to expanding the supply of affordable housing in Australia: an increasing role for the private sector | <p>Final report assessing the challenge of achieving greater private sector involvement in the financing of affordable housing.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=42</p> |
| A spatial analysis of trends in housing markets and changing patterns of household structure and income | <p>Provides a spatially disaggregated analysis of housing system change 1986-96 and examines the housing outcomes associated with such demographic, economic and social change.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=8</p> |

| Title | Summary |
|--|---|
| A Microsimulation Model of the Australian Housing Market with Applications to Commonwealth and State Policy Initiatives | <p>This paper aims to compose a microsimulation model capable of measuring the impact of Commonwealth and State government housing programs on the prices that households pay for housing, and the subsidies they receive.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=17</p> |
| A distributional analysis of the impact of direct and indirect housing assistance | <p>This study will provide a comprehensive assessment of the distributional impact of the major forms of broadly defined housing assistance provided by the Commonwealth and will provide an assessment of the extent to which the changes in the different forms of housing assistance have contributed to improved targeting of that assistance.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=12</p> |

Current Projects

| Title | Summary |
|--|---|
| Falling through the net? A risk management model for home ownership support schemes | <p>Provides tools for all the SHAs in Australia to more cost effectively manage risks when they operate home ownership support programs.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=14</p> |
| Explanations of changes in housing tenure in Australia | <p>This project aims to document and explain trends in home ownership across time, especially in the 1990s with a view to the implications for the future.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=31</p> |
| Regional Impact of Rent Assistance | <p>Development of a microsimulation model to analyse at small area level the performance of Commonwealth Rent Assistance.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=10</p> |

| Title | Summary |
|--|---|
| Financing affordable housing: a critical comparative review of the UK and Australia | <p>Critically compares the debates, research findings and policy developments directed towards attracting private investment into affordable housing provision in Australia and the UK.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=95</p> |
| What drives housing outcomes in Australia? Understanding the role of aspirations, household formation, economic incentives and labour market interactions | <p>Development of an integrated model of the housing system that incorporates the broad range of drivers that influence the housing market.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=67</p> |
| Affordable housing and employment opportunity: is there a spatial mismatch? | <p>Maps the distribution of housing affordability, unemployment concentration and employment location in Melbourne to assess patterns of spatial mismatch.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=96</p> |
| A practical framework for expanding affordable housing services in Australia: learning from experience | <p>Uses case studies to assess established project and organisational models of affordable housing to determine their appropriateness in the Australian institutional, policy and investment contexts.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=94</p> |
| Rent assistance and the spatial concentration of low income households in metropolitan Australia | <p>Explores spatial trends in the provision of low income rental housing in Melbourne and Sydney concentrating on the relationship between Rent Assistance and locational choice.</p> <p>http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=100</p> |

| Title | Summary |
|--|--|
| Changes in the supply of and need for low rent dwellings in the private rental market | <p data-bbox="679 230 1406 360">Analyses 2001 census data to determine the mismatch (or otherwise) between the supply of and the need for low rent housing.</p> <p data-bbox="679 398 1406 472">http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=99</p> |
| Housing and community in the compact city | <p data-bbox="679 506 1406 689">Investigates the process by which households with limited resources are excluded from high amenity areas and gravitate to areas offering relatively low housing costs.</p> <p data-bbox="679 728 1406 801">http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=98</p> |
| Baseline small area projections of the demand for housing assistance | <p data-bbox="679 835 1406 1066">Broadens the parameters of AHURI project <i>The Regional Impact of Rent Assistance</i> to provide baseline projections for small areas (i.e. Local Government Areas) of potential demand for Housing Assistance by household characteristics.</p> <p data-bbox="679 1104 1406 1178">http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=88</p> |
| Ageing in place? Intergenerational and interfamilial housing transfers and shifts in later life | <p data-bbox="679 1211 1406 1395">A national study of the economic and social circumstances of people at mid-life in order to predict future demands and capacities to pay for housing and other services.</p> <p data-bbox="679 1433 1406 1507">http://www.ahuri.edu.au/publish/page.cfm?contentID=30&projectid=91</p> |

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