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Housing risks 'catastrophic': Grattan Institute

By Peter Martin
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Australia's eight-year house price boom has savaged the living standards of poorer Australians while so far leaving the wealthy untouched, a new Grattan Institute analysis finds.

But the report, to be released on Monday, warns of a "catastrophic" impact on all income groups should mortgage rates rise by more than a few percentage points.

Home building has fallen behind population growth pushing up prices.
Photo: Scott McNaughton

The institute’s chief executive, John Daley, said Australians who already owned their houses had been little affected by soaring prices to date because they had been “hedged”. If they moved, they could buy again for about the price they got when they sold. Property investors had done well out of the explosion in Sydney and Melbourne prices because they had always been planning to sell.

But new buyers had been locked out.

Home ownership had plummeted among Australians aged 25 to 34, sliding from 61 per cent in the early 1980s to just 44 per cent in the most recent census. Ownership among Australians aged 35 to 44 had plunged from 75 to 62 per cent.

Although ownership rates among older Australians had held up to date, outright ownership was slipping. The proportion of Australians aged 55 to 64 who own houses mortgage-free has slipped from 72 per cent to 42 per cent since the late 1990s. The proportion of Australians aged 65 and older who are mortgage free has slipped from 82 to 75 per cent.

“Some of these older households will, quite rationally, use some or all of their superannuation savings to pay off their mortgage debt,” Mr Daley says in the report. “This undermines the intent of the super system, and means that its substantial tax concessions are never used to reduce age pension costs.”

Even a modest increase in interest rates could stretch many Australians.
Photo: Paul Rovere

The report finds the bottom fifth of Australian earners are paying 28 per cent of their disposable income in housing costs (either in rent or mortgage payments), up from 24 per cent eight years ago. By contrast, the top fifth are paying 10 per cent, scarcely any more than they were before prices took off.

The unchanged circumstances of high earners reflect much lower interest rates, which until now have offset the effect of higher prices.

Low earners have suffered from a flood of investors into cheaper suburbs where they have pushed up prices in order to take advantage of negative gearing and avoid high land taxes.

Forty-four per cent of low earners are in rental stress, up from 35 per cent eight years ago.

Mr Daley warned that the Australians who had so far escaped higher housing costs were in for a shock when interest rates recovered from their historic lows.

“A 2 percentage point rise would be catastrophic for most new home owners,” he said. “It would be much more catastrophic than in the past, because when you start on a 3.5 per cent interest rate and go to 5.5 per cent, the increase in payments is huge."

In addition, mortgage holders could no longer safely assume that mortgage payments would shrink over time as a proportion of their income as wages grew. Higher mortgage rates combined with much slower wage growth could see them remaining mortgage holders for much longer.

The Howard government’s decision in the late 1990s to halve the headline rate of capital gains tax was responsible for much but not all of the blowout in prices by making negative gearing more attractive. The report recommends that the 50 per cent discount on capital gains tax be phased down to 25 per cent.

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>
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Much of the rest of the blowout was caused by home building falling well behind population growth.

“It’s all very well running a strong migration program,” Mr Daley said. “But if you don’t build enough dwellings to back that up, the price of housing goes up. It’s not surprising.

“For much of the decade from 2005 to 2014, annual housing construction was at or lower than the average of the previous 25 years, but with population substantially higher, around 350,000 per year rather than 220,000 per year,” the report says.

“The share of Australia’s population living in our four largest cities is expected to increase from 58 per cent today to 66 per cent by 2061. The population of Melbourne is expected to climb to almost 8 million by 2051. Sydney’s population could climb to 8 million by 2056.”

Mr Daley said the “first best” policy was to run a strong migration program and build enough extra homes, as had happened in the past. Australia took in a large number of migrants in the 1950s with no material jump in home prices, because it built a lot of houses.

“Right now we are in a third best world, which is to have a really strong migration program while keeping the clamps on planning rules and land release, so that we can’t house them. Our young people are paying for that.”

The report recommends the Commonwealth use ‘carrots and sticks’ to encourage states and local governments to allow much denser housing, especially along transport corridors. Local councils that failed to meet density targets would lose their planning powers.

Residents who opposed denser housing should be told that without it, their children would most likely be unable to buy a home. They should also be told that without denser housing, including denser housing for aged residents, they would have to leave their suburbs when they became infirm.

In a prepared response to the report, Treasurer Scott Morrison seized on the finding that capital gains tax was not the only reason prices had been climbing, saying that Labor’s proposal to wind back the concession was a “blatant tax grab”. His response did not address the findings about planning.