Keeping a roof over your debt

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Sydney's higher house prices over the past four years have seen many householders take on larger mortgages while remaining in their own home.

And it has been high-debt households that have increased their debt by more than low-debt households.

Research by the Australian Housing and Urban Research Institute (AHURI) has suggested the response of households to house price growth has been greatest among households with already higher levels of indebtedness. "These households are the most vulnerable to income shocks, such as unemployment," the report warned.

It found that a $1000 increase in house values prompted a $240 increase in household debt for homeowners. A 1 per cent increase in local house price growth was accompanied by a 0.3 per cent decrease on household non-mortgage debt.

The report warned the take-up of further mortgage debt exposed them to the risk of significant loss if house prices fell or if interest rates rose.

"This, in turn, may pose a systemic risk for the macroeconomy. An economic shock, emanating in either financial, labour or housing markets, may lead to widespread defaults that would cause the shock to spread across markets and threaten the performance of the economy," it said.

The report noted a belief in Australia that debt is held by those most able to service it, namely higher-income and higher-wealth households. The Organisation for Economic Cooperation and Development has long observed that Australia's household debt ratios (debt divided by disposable income) are high by international standards.

In the mid-1990s, household debt was around 50 per cent of household disposable income. This ratio rose to over 150 per cent of income by 2007, with housing debt alone accounting for almost 90 per cent of this, and has since remained constant.

In Australia we have not seen households reducing their debt burden as witnessed in other countries more severely affected by the GFC.

Instead when these households experienced increases in their housing wealth, they have been quite likely to refinance from their relatively more expensive unsecured non-mortgage debt, by moving debt from credit card to home loan. The debt escalation is possibly already adding to housing stress and resulting in less money being available for spending.

We know around 30 per cent of homeowners have no debt, but evidence on the relationship between house prices and debt is scarce.

There are always links between household debt and work life-cycle.

Any price movements in housing markets have the potential to either promote or dampen labour supply, according to the AHURI research paper, House prices, household debt and labour supply in Australia, authored by Kadir Atalay, Garry Barrett and Rebecca Edwards.

Higher housing debt-to-income levels are associated with longer working hours.

But throw in the positive wealth effect of good house price growth and it leads to a reduction in labour supply for older women via early retirement and for young partnered men and women who move to carer activities.

Anticipated changes in wealth are built into consumption plans, but unemployment shocks aren't.

It was interesting to see more borrowers are falling behind on repayments, according to credit ratings agency Fitch this week.

Despite low interest rates, the appreciating housing market and falling unemployment, Fitch believes the worsening arrears may be due to the emerging trend of higher underemployment.