POLICY EVIDENCE SUMMARY

July 2023

Achieving home ownership: comparing experiences across generations

Based on AHURI Final Report No. 404: Transitions into home ownership: a quantitative assessment

What this research is about

This research analyses the economic constraints on people's ability to buy a home over the four decades from the early 1980s. It analyses how home ownership has evolved over time; considers demand subsidies provided to first homebuyers; and examines the support from other family for first homebuyers.

The context of this research

Home ownership rates for people aged 30 have fallen from a high of 65 per cent among those born in the late 1950s to around 45 per cent among those born in the 1980s. This development reflects a range of social, demographic and economic influences. Coinciding with the decline in housing affordability, successive cohorts of Australians have entered home ownership at lower rates at any given age.

In the presence of imperfect credit markets and constraints on borrowing against future earnings, households face constraints on financing the debt of housing they intend to occupy: generally characterised as the deposit or downpayment requirement, and debt-servicing limits. Both constraints limit the magnitude of housing services that aspiring first homebuyers (FHBs) can purchase.

The key findings

Lower home ownership rates over time represent a delay as well as a decline

This report highlights that the lower rates of home ownership achieved by successive cohorts of younger Australians represent, in part, simply a delay in entry into home ownership. Younger cohorts that experience lower levels of home ownership at ages 30–34 years do exhibit some catch-up over time—in other words, home ownership rates of that group as they age approach the home ownership rates of older cohorts. However, that catch-up remains incomplete. After 10 years, less than half of the gap at age 30–34 years has closed, and between two-thirds and three-quarters of the gap is closed after 20 years.

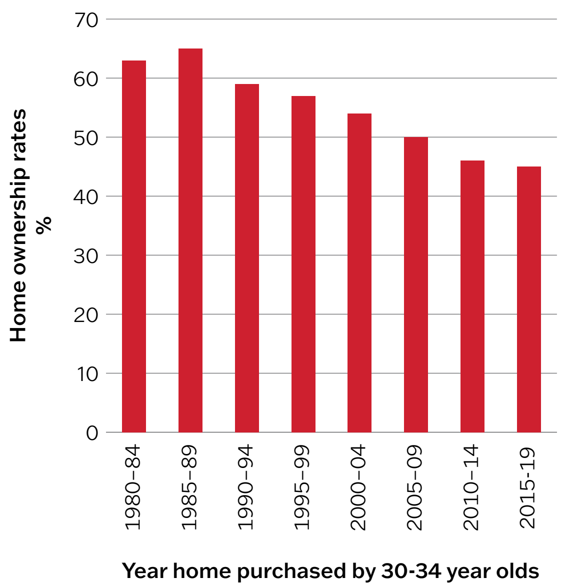
The timing of the decline in the home ownership rate at age 30 over recent decades coincides with the sharp increases in Australian house prices. This suggests that rising house prices may be a contributing factor in the significant variation in young people's ability to buy a home over the decades.

Recent households less likely to own a home at 50 than for previous generations

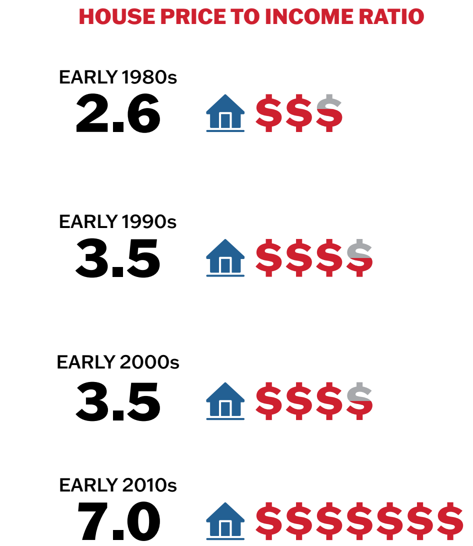
Importantly, those birth cohorts that were less likely to get onto the ladder at younger ages only partially catch-up with older cohorts. This means that the gap in ownership rates across cohorts remains even when measured at age 50. Empirical analysis shows that 25 per cent of the overall gap in home ownership rates at ages 30–34 remains after 20 years. Combined with the relatively modest increases in home ownership rates from age 50 onwards, these findings suggest that there are concerns regarding falling living standards and poverty among the retired who have not attained home ownership.

Homeownership rates are on the decline, and median house prices are on the rise

The home ownership rate among 30-34 year olds is falling



The median house price has increased significantly relative to the median income of 30-34 year olds over the past four decades



Source: AHURI Final Report No. 404

Different measures of 'unaffordable housing' include households' reduced ability to save for a deposit or to make mortgage repayments

The 'cost' or affordability of owner-occupied housing reflects a range of factors, not simply the 'purchase price' of the dwelling. Households buying a dwelling generally finance it through a mortgage. Due to the nature of imperfect credit markets, financial institutions generally impose a series of conditions on households that wish to borrow funds, each of which potentially impacts on the affordability of housing. These conditions include:

- the requirement for a deposit to demonstrate a capacity to save and defer consumption
- limits on the size of the mortgage loan relative to the purchase price
- a requirement for lenders insurance (in some cases).

Together, these factors influence the affordability of housing along with broader economic or market conditions.

In Australia, the most important financial market condition is the level of interest rates on home loans (which are typically for 20–30 years). While Australian home loans traditionally had variable interest rates, fixed-interest rate loans also became available from the early 1990s. For a mortgage debt, the interest rate will impact the loan repayments required to extinguish the mortgage over the term of the loan and the borrowing capacity of the household. While interest rates have declined over the past decade to historic lows this has been offset by other developments such as increases in house prices and more stringent prudential regulations limiting the size of loans.

There are a range of alternative ways to measure housing affordability. A simple metric measures the price of housing relative to household income. Typically, house prices in Australia throughout the 1990s were two to three times average annual household incomes. An increase in this ratio is consistent with a deterioration in affordability, as the capacity of a household on a given income to service a mortgage will decline as house prices increase, if all other things remain the same.

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A similar pattern emerges when considering an alternative measure that focusses on assessing the time required to save for a deposit for a 'typical' dwelling for an 'average' household. This is an important challenge faced by first homebuyers, namely the requirement to accumulate savings for a deposit. In the period 2020–2021, the time required to save a 'typical' deposit has increased in all capital cities (except Brisbane) by an average of four months.

The mortgage debt-service ratio incorporates the effect of interest rates on housing affordability by calculating the monthly required repayment on a new mortgage divided by monthly disposable income. Over time, the aggregate mortgage debt-servicing ratio across the economy has varied but in general remains below historical peaks in the late 1980s and the mid-2000s.

Households wanting to buy a home may also respond to unaffordable housing by purchasing housing of a lower quality or quantity; deferring the transition into home ownership; or turning to alternative sources of funding, such as parental transfers.

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New ways to borrow money led to higher house prices and higher household debt

Traditionally, mortgages in Australia took the form of a fully documented, full-recourse, variable-rate loan from a bank. The entry of non-bank lenders led to the development of new products such as interest-only loans and revolving credit lines. Lending standards tended to be relatively stringent prior to the deregulation of the 1980s, with a loan-to-value ratio of 80 per cent and debt-to-income limits commonly applied by financial institutions.

The availability of relatively cheap credit coincided with an increase in the size of mortgages both in an absolute and relative sense, which left household debt to GDP in Australia among the highest across OECD economies. As the set of loan instruments on offer expanded, there is evidence that first homebuyers tended to choose products that provided opportunities to access home ownership with lower downpayments and fixed or 'honeymoon' interest-rate loans.

Intergenerational financial support: parents to the rescue

There is increasing evidence in Australia and internationally that parents represent an important source of finance for the purchase of owner-occupied housing.

As house prices have increased, this has led to substantial increases in the housing wealth of existing home owners —especially older home owners. Coupled with financial innovations that have allowed households to draw on housing equity, parental transfers—both inheritances and financial gifts—appear to have become one of the key enablers of the transition into home ownership.

There is less evidence of the role played by in-kind transfers such as co-residence. Residing with parents offers young adults the opportunity to share housing-related costs and accumulate savings. In doing so, it potentially provides an important mechanism to facilitate entry into home ownership. Statistical analysis highlights that additional time spent co-residing with parents is associated with higher transition rates into home ownership in the order of 50 per cent, relative to those who are privately renting. Family support may also be important in light of labour market insecurity that makes it more difficult to accumulate savings for a deposit in a way that previous generations were able to.

One consequence of intergenerational transfers from parents to children is the potential impact on the wealth of recipients and, more broadly, the level of inequality. An examination of 15 European countries finds that intergenerational transfers represented approximately 10 per cent of net household wealth on average, highlighting the importance of home ownership for the accumulation of wealth.

Reliance on demand subsidies for first home buyers has failed to support home ownership

Over the past four decades, governments have increasingly relied on demand subsidies or concessional tax settings for first homebuyers to assist entry into home ownership. Demand subsidies are unlikely to benefit those seeking to enter into home ownership as they tend to increase prices paid by buyers. There is empirical evidence that such subsidies simply bring forward the purchase of owner-occupied housing rather than increase rates of home ownership. Indeed, there is a broad consensus that such policies tend to be absorbed into higher house prices or simply lead to a faster transition into owner-occupation among those who would have achieved that outcome anyway.

What this research means for policy makers

There is increasing evidence that home ownership is not simply delayed but rather it will not be attained by a large set of individuals. This increasing inequality does has important implications for the welfare and wellbeing of Australians as they move into retirement, and presents challenges for the current transfer system, which has high rates of home ownership in retirement as one of its pillars. This also speaks to broader issues around the treatment of owner-occupied housing in the tax and transfer system.

Policy measures should be targeted at individuals who may not otherwise attain owner-occupation because of credit-market constraints or the absence of alternative forms of assistance such as familial transfers. Moreover, given the specific financing challenges associated with the purchase of a dwelling, those measures should focus on credit-market imperfections that limit the capacity of households to achieve their desired tenure status.

It is critical that such policies be considered in light of the risk that home ownership may create for individuals and the broader economy. Those policies should be measured and targeted, while ensuring that home ownership is accessible to those that seek it.

Policy settings should also recognise that not all individuals will seek to attain home ownership, nor should they be encouraged to attain it. While owner-occupation presents benefits such as security of tenure, it also comes with costs and risks to the individual. Moreover, it is important to recognise that there are alternative opportunities other than through home ownership to save and accumulate wealth over the life cycle.

Methodology

This research uses statistical or econometric methods to provide insights into the housing behaviours and outcomes of Australians over time. The research uses data from the Survey of Income and Housing (SIH) and Household Expenditure Survey (HES), conducted by the ABS, using data from 1984 to 2017. The analysis also used the Household Income and Labour Dynamics in Australia data.

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To cite the AHURI research, please refer to:

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Available from the AHURI website at ahuri.edu.au/research/final-reports/404