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EXECUTIVE SUMMARY

# Moving, downsizing and housing equity consumption choices of older Australians

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# Executive summary

## Key points

The Australian population is ageing, and this presents both challenges and opportunities for Australian policy-makers. The key challenge is that there are likely to be increasing fiscal demands from an older demographic for services such as long-term care and programs such as the Age Pension (AP). On the other hand, there are opportunities to meet this challenge. The opportunities are made available via the high rates of home ownership and related high levels of housing wealth of older Australians. This accumulated wealth provides governments and individuals with the means to maintain appropriate levels of consumption throughout retirement, thus minimising reliance on government support. By implementing appropriate policy development, governments can assist older Australians to make geographic mobility and downsizing decisions that ensure they are housed appropriately, according to their needs and circumstances, as they age.

This study analyses current geographic mobility and downsizing behaviours among Australians aged over 55. Key findings include the following.

- Few Australians aged over 55 years move homes on an annual basis.
  - Geographic mobility declines with age and is higher among renters—varying from 3 per cent per annum among owner-occupiers aged 75 years and over, to around 18 per cent among renters aged 55–64 years.
- An analysis of barriers to geographic mobility identified by a set of older Australians highlights that the majority of individuals report either health or affordability as the primary barrier to moving.
- Downsizing behaviour is generally correlated with specific life events, such as change in partnership status, adult children leaving the parental home, or change in health status.
- Evidence suggests that the AP assets test (but not the AP income test or age eligibility rules) discourages downsizing.
- Among older Australians, both geographic mobility and downsizing are associated with an increase in financial and life satisfaction, but a decrease in housing and neighbourhood satisfaction.
- Negative impacts of moving on wellbeing, as measured by satisfaction, appear to moderate over time, potentially reflecting individuals' adaptation to their new living arrangements.

Like other developed countries, Australia faces economic and fiscal challenges associated with demographic changes posed by an ageing population. Central to this issue is the need to ensure that housing markets function efficiently and facilitate housing choices or adjustments that meet the needs of older Australians. Such an outcome is critical, not simply for the welfare of older Australians, but to ensure the efficient functioning of the economy more generally.

A key concern in this context is whether—and by what means—older Australians are able to adjust their housing consumption so that it matches their housing and non-housing needs at a critical part of the life cycle. Such changes are commonly referred to as ‘downsizing’. Transitions into retirement and other major life events, such as changes in health and the departure of dependent children from the family home, have important implications for the housing needs and aspirations of older Australians. Moreover, the wealth locked up in housing assets provides an opportunity to meet the non-housing consumption needs of older Australians.

These issues are likely to become more pronounced in Australia in coming years, as individuals and governments face the fiscal challenges associated with an ageing population that requires additional expenditure while the proportion of working individuals shrinks.

The central aim of this report is to describe the nature of downsizing decisions, along with the facilitators, barriers and consequences of those decisions.

## Key findings

The research team analysed quantitative data from a variety of sources to address the research questions, including the Survey of Income and Housing (SIH), the Household, Income and Labour Dynamics in Australia (HILDA) Survey, and the Australian Census Longitudinal Dataset (ACLD).

Over the past five decades, owner-occupation has been the dominant form of housing tenure for Australians. Housing careers (i.e. the movement of a household into different tenures across the life-cycle) often involved a transition from the parental home around the time an individual partnered or completed their full-time education. Typically, a spell of rental tenure was followed by the purchase of a home, and this provided an opportunity to accumulate wealth, in the form of housing equity, over the course of the individual’s working life. Until the early 2000s, upon entering retirement individuals were generally mortgage free, and owner-occupied housing represented an important source of welfare during retirement. This pattern was particularly important in light of the limited availability of superannuation for older generations and the relatively low rate at which the AP was paid.

Analysis of the SIH highlights important developments that younger generations have experienced in terms of their housing careers. Although we do not observe significant differences across cohorts in rates of home ownership, there is evidence that fewer individuals in more recent birth cohorts are outright home owners relative to their older counterparts. Hence, many elderly individuals now enter their retirement years while holding significant mortgage debt. Given the maturation of the superannuation system and the rules embedded in the current AP system, this has potential implications for older Australians, who will face a number of decisions upon retirement. Households that have not paid off their home could, for example, choose to transfer assets across their portfolio at the time of retirement to eliminate their mortgage debt. By doing so, individuals and households could potentially maintain access to the means-tested AP. Alternatively, they could choose to reduce or eliminate mortgage debt by downsizing. How retirees’ decision-making behaviours in this area evolve over time may have important implications for government finances and the sustainability of the tax and transfer system.

Like many developed countries, there is evidence that Australians tend to retain high levels of housing wealth throughout their retirement. This is consistent with a pattern whereby individuals choose not to downsize: neither by moving to a smaller dwelling (downsizing in a physical sense) nor by transitioning to a dwelling of lower value (financially downsizing). Analysis of the

HILDA data indicates that among owner-occupiers in 2001 aged over 54 years, more than 75 per cent remained in the same dwelling 15 years later. While downsizing in a financial sense is somewhat more common than physical downsizing, both scenarios remain the exception among older Australians rather than the norm. For example, among all age groups 55 years and older, fewer than 20 per cent of individuals had transitioned into another owner-occupied dwelling and reduced their net level of housing equity in the process.

International research suggests that geographic mobility and downsizing behaviours are often associated with demographic and work transitions. Evidence from the HILDA data and the ACLD confirms these patterns for Australia. In particular, we find several important factors associated with housing mobility at older ages in Australia, including demographic transitions (particularly those associated with partnership status or children leaving home), and labour force transitions (primarily at the age of retirement).

Among those individuals who do downsize, there is little evidence that their financial wellbeing and overall satisfaction improves as a direct result. Analysis of the HILDA data indicates that reported satisfaction with housing circumstances immediately following the move actually decreases. However, this appears to represent a temporary shock, perhaps associated with the substantial disruption to social and community ties that occurs when an older individual moves. Unsurprisingly, downsizing behaviour is generally associated with a significant rebalancing of the household portfolio, with an increase in wealth held in the form of liquid financial assets.

The conceptual framework that shapes the analysis in this report is the life-cycle hypothesis (LCH), which posits that individuals plan their consumption and savings behaviour over their life-cycle. A key consideration in this context is how economic constraints, such as tax and transfer rules, shape decisions over the life cycle. This is particularly pertinent in the Australian context given the unique nature of the AP program and the generous treatment of owner-occupied housing in the tax system. Analysis of the HILDA data shows some evidence that decision-making around geographic mobility and downsizing is associated with parameters of the AP means test. In particular, we observe that individuals who are not at risk of losing their eligibility to AP benefits are more likely to move, relative to individuals who are at risk of losing eligibility.

## Policy development options

This report does not focus on a single economic policy that may facilitate or represent a barrier to downsizing behaviour among older Australians. Rather, the analysis provides an opportunity to understand the patterns of downsizing that occur, how these patterns have changed over time, and how they may be shaped by a range of economic factors. The analysis provides insight into how policy may be formulated in a way that limits the barriers to downsizing for older Australians, facilitates housing choices that are appropriate at each stage of the life cycle, and provides an opportunity for governments to address approaching fiscal challenges.

A review of the literature identifies patterns, observed both in Australia and internationally, that highlight the relatively limited degree of downsizing engaged in by older households. Like their international counterparts, older Australians do not tend to decumulate housing wealth as they enter into the retirement part of the life cycle. Rather, they tend to ‘age in place’,[1] and downsizing behaviour tends to be associated with significant life events, such as the death of a spouse, retirement, or a health scare. The economic approach argues that downsizing behaviour is likely to be driven, at least in part, by the costs and benefits associated with

[1] Remain in one’s own home after retirement; not move into a smaller home, assisted living, or a retirement community.

alternative arrangements. Those costs and benefits will in turn be shaped by the policy context in which housing decisions are made, including tax and transfer policies. The analysis in this report suggests that tax policy may have a limited impact on downsizing decisions. Nonetheless, over the life cycle, it is likely that tax and transfer policies will form an important component of any policy actions directed towards shaping the downsizing behaviours of older Australians.

The current settings with respect to owner-occupied housing, in the Australian AP program and the tax system more generally, are relatively generous. They provide clear incentives for individuals to retain relatively large amounts of wealth in the form of housing equity in owner-occupied housing over the course of the life cycle, and a larger share of their wealth in housing equity than they would if housing were treated more neutrally relative to other assets. Recent changes to the AP assets test have meant that some AP recipients, especially homeowners with above average levels of wealth, will have received lower levels of AP payments (Australian Council of Social Service 2015a). The experience of the past 30 years (following the introduction of the AP assets test in 1985), suggests that—notwithstanding a consensus from commentators on both sides of the political divide that changes in the treatment of housing assets are justified—any such changes are likely to be adopted slowly. Moreover, a gradual approach is most likely the appropriate one. Choices around housing are critical from a life-cycle perspective and changes to policy should be introduced progressively to ensure that the parameters that shape life-cycle decisions can be adequately incorporated into long-term planning horizons.

Thus, we pose the question: 'What is the nature of the policy changes that may be justified?' There is a broad consensus among policy makers that housing is treated relatively generously from a tax perspective. This has important implications in terms of efficiency, as it potentially provides an incentive for individuals to rely too heavily on housing assets over the course of the life cycle. Moreover, from an equity perspective, one may argue that generous tax concessions available to older owner-occupiers provide the greatest benefit to those who already exhibit relatively high levels of accumulated wealth.

A number of changes could be made to the AP assets test regime, to make owner-occupied housing less attractive in a financial sense. For example, current thresholds that apply to the AP assets test mean that the implicit value of owner-occupied housing is equal to approximately \$200,000[2]; an adjustment of those thresholds could make owner-occupied housing less attractive and encourage individuals to rebalance their wealth portfolio over the life cycle. While this approach may be appealing, it is important to note one unintended consequence of such a policy: if the assets test threshold is lowered for home owners, it may reduce the incentive for existing owners to downsize, unless the proceeds from such an action are treated in a concessional manner. Of course, such a change has the potential to increase the fiscal burden associated with the AP by extending access to the publicly funded pension. A recent policy announcement revealing the option to top-up superannuation using the proceeds of downsizing is an example of such an approach. It is important to recognise that past experience would suggest that such policies tend not to be broadly embraced by individuals.

History tells us that for policy changes to be effective, they must be made with a life-cycle perspective in mind. Australians who are currently retired or near retirement have made saving and consumption decisions based on a set of tax and transfer parameters that should only be altered with careful consideration of the consequences.

[2] The AP assets test allows non-home-owners to hold approximately \$200,000 more in assets than home owners before the amount of AP collected is affected.

Finally, it is important to note that any changes to economic policies, such as tax and transfer arrangements, will likely only impact those individuals who are characterised as being at the margins. For example, a change to assets test thresholds for the AP generally affects the behaviour of those whose asset holdings are at or near the threshold the behaviour of others is unlikely to be impacted. In effect, without a large policy shift that fundamentally changes the costs and benefits associated with the accumulation of housing assets by older Australians, policy changes are likely to affect a relatively small subset of the cohort and change the behaviour of only a proportion of these. On the other hand, fundamental change will take both time and substantial policy reform. Furthermore, developing a political consensus around such changes is likely to require time and a concerted effort on the part of policymakers. To make a meaningful difference to behaviour and outcomes, policies must be well thought-out, pre-announced to allow for forward planning, and supported to remain in place long term.

## The study

The research questions addressed in this report were shaped by the economic and fiscal challenges posed by an ageing population. As the Australian population ages, governments will be faced with increasing fiscal pressure to fund programs and expenditures demanded by older Australians; at the same time, relatively few younger Australians will be engaged in the labour force and paying tax.

The analysis examines the behaviour of Australians aged 55 and over in relation to two factors that are critical to meeting the challenges of an ageing population: downsizing and geographic mobility. The research examines a series of related, but nonetheless distinct, questions.

- What patterns are evident in the owner-occupation and equity withdrawal behaviours of older Australians since the 1990s? To what extent do such patterns reflect cohort influences? What are the implications for the future?
- What is the nature of downsizing that occurs among older Australians who move, in terms of changes in housing size and value?
- What are the characteristics and circumstances of older Australians who exhibit geographic mobility?
- What happens to the financial and general wellbeing of older home owners who downsize or move? How are the asset portfolios of these households affected?
- How do the parameters of the tax and transfer system influence decision-making around geographic mobility and downsizing among older Australians?
- What are the other key factors associated with the geographic mobility behaviours of older Australians?

An ageing population is a problem shared by many countries. While a range of policies have been put in place in Australia to encourage individuals to remain active in the labour force, the role of housing in meeting this challenge has not been systematically addressed. Housing equity is a form of accumulated wealth that remains largely untapped during retirement years, and there is potential for the consumption of this wealth by older Australians to relieve the fiscal pressure faced by future governments. Policies acting to implement such an approach may have broader implications; for instance, ensuring a more appropriate match between the housing needs and outcomes of not just older Australians but also younger Australians. Hence, policy changes aimed at shaping downsizing behaviours have the potential to ensure a more efficient allocation of housing stock across cohorts of Australians. Ultimately, such an outcome will be conducive to greater economic efficiency and welfare.

The methodological approach in this report is economic in nature and draws on the insights provided by life-cycle models of behaviour. Such models are predicated on an assumption that that individuals are forward-looking agents, and that choices around work, consumption and saving are shaped by inter-temporal trade-offs. Moreover, those trade-offs are impacted by economic, social and institutional considerations. Tax and transfer policies have important implications for the costs and benefits associated with alternative choices and therefore have the potential to influence behaviours and outcomes. The analysis undertaken for this study is quantitative or statistical in nature. The analysis of the HILDA dataset, the ACLD and the SIH data allows patterns of geographic mobility and downsizing behaviours among older Australians to be described and analysed. The analysis is Australia-wide in its coverage, and mostly considers the period from 1994 to the present. The analysis of the HILDA dataset focusses on the period since 2001 only.

By drawing on the strengths of each of the datasets used, the analysis in this report provides a number of original contributions. The repeated cross-sectional nature of the SIH provides an opportunity to consider how housing-related decisions of successive cohorts of older Australians have evolved over time. The rich set of social, demographic and economic information in the HILDA dataset provides an opportunity to identify, using robust statistical techniques, the correlates of downsizing behaviour, along with the consequences of geographic mobility and downsizing. In addition, the longitudinal nature of the HILDA dataset provides an opportunity to consider the extent of geographic mobility and downsizing behaviours over the life cycle. Finally, use of the ACLD provides an opportunity to identify the nature and extent of downsizing behaviours for a large sample of older Australians.

Overall, the report’s findings add to the existing evidence base around which robust policies designed to facilitate geographic mobility and downsizing can be formulated.

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## HILDA Survey

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