

# **Affordability and access to home ownership: past, present and future?**

**National Research Venture 3: Housing  
affordability for lower income Australians**

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authored by

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## **DISCLAIMER**

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# CONTENTS

<b>LIST OF FIGURES .....</b>	<b>III</b>
<b>EXECUTIVE SUMMARY .....</b>	<b>1</b>
<b>1 THE CHANGING DREAM .....</b>	<b>4</b>
1.1 The 1950s and 1960s dream .....	5
1.2 The 1970s and 1980s dream .....	6
1.3 The 1990s and 2000s nightmare .....	8
<b>2 IMPLICATIONS.....</b>	<b>12</b>
<b>3 FAIRNESS AND HOUSING.....</b>	<b>17</b>
3.1 Defining a fair housing system .....	17
3.2 Defining a fair housing assistance system.....	17
3.3 The current housing assistance system.....	18
<b>4 CONCLUDING REMARKS.....</b>	<b>19</b>
<b>REFERENCES .....</b>	<b>20</b>

## LIST OF FIGURES

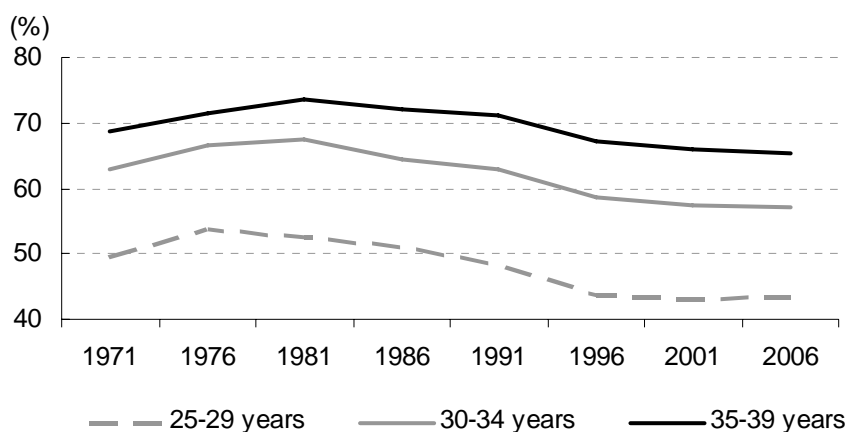
Figure 1: Home ownership rates over time for younger households by age cohort.....	4
Figure 2: House price to income ratio .....	9
Figure 3: Deposit gap to income ratio .....	10
Figure 4: Real private sector wealth per head (\$2003/04).....	13
Figure 5: Household net worth by age of reference person, 2003/04.....	14
Figure 6: Household net worth by age of reference person and tenure, 2003/04.....	15
Figure 7: Household net worth by net worth quintile, 2003/04.....	16

## EXECUTIVE SUMMARY

Whilst it might be dangerous to use the past to predict the future, it is equally dangerous to ignore the lessons of yesterday in determining what might happen tomorrow. This paper examines the implications for young adults of the changing patterns of investment in housing over several generations. It provides a brief snapshot of three distinct phases in the evolution of home ownership: as an aspiration of households in the 1950s and 1960s, as a driver of inequality for their baby boomer children in the 1970s and 1980s, and as a fading dream of their grandchildren from the 1990s to the present. It begins with the rise of home ownership in the immediate post-WWII period and ends with the rise in rental investment that dominated the most recent house price boom.

A key concern, identified in Chapter 1, is the decline in home ownership rates for younger households over the past 30 years.

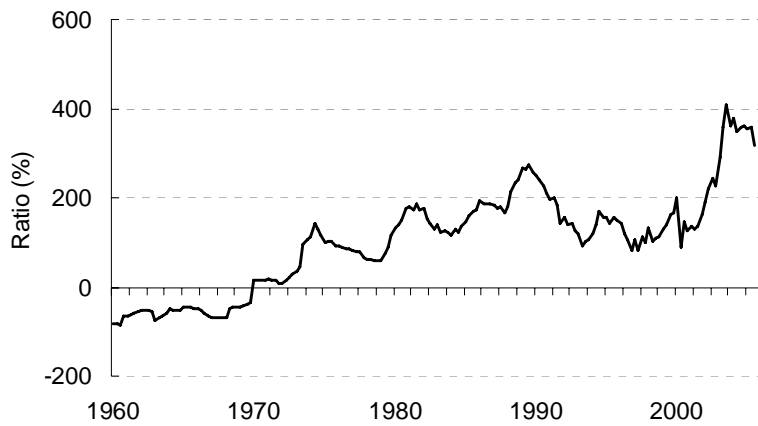
### Home ownership rates over time for younger households by age cohort



Chapter 1 focuses on the relationship between housing affordability and access to home purchase for first home buyers. It employs a deposit gap measure to show that the decline in affordability for those on the equivalent of average weekly earnings began as far back as 1970.

It suggests that the switch from the 1960s, when it was possible for a household on average earnings to borrow enough to purchase a dwelling without a deposit, to the 1970s and 1980s, when a deposit of at least double annual income was required before a household on average earnings could afford a median-priced dwelling, coincided with a change in focus from the security and shelter provided by owner-occupied housing to the potential it provided for wealth accumulation. At present the deposit gap is at least four times the income of those on average earnings. This suggests that, to gain the same level of access as their parents and grandparents, the current generation will need considerable assistance.

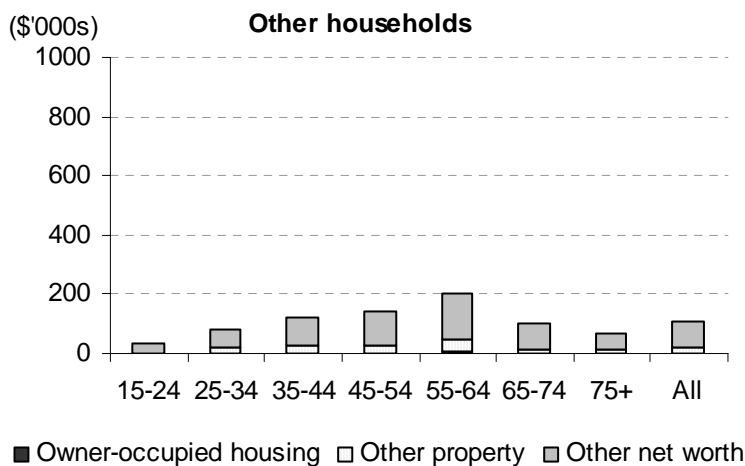
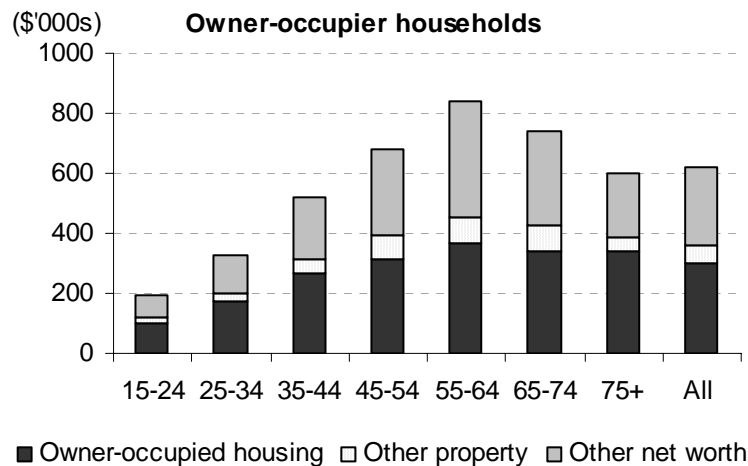
### Deposit gap to income ratio



Chapter 2 provides data on the distribution of wealth. These show the significant inequalities that exist between those who do and those who do not own their own homes, as well as the even more extreme inequalities that exist within the distribution of wealth.

They suggest that parents or grandparents who did not achieve home ownership are unlikely to have sufficient resources to assist their descendants. This highlights the potential of home ownership to add to wealth inequality.

## Household net worth by age of reference person and tenure, 2003/04



Chapter 3 argues that affordability problems and lack of access to owner-occupied housing are essentially problems of income and wealth distribution that can be redressed only if they are tackled as such. The paper provides a brief overview of the distributional characteristics of the current system of housing assistance and outlines characteristics that would be needed to make the housing assistance system fairer.

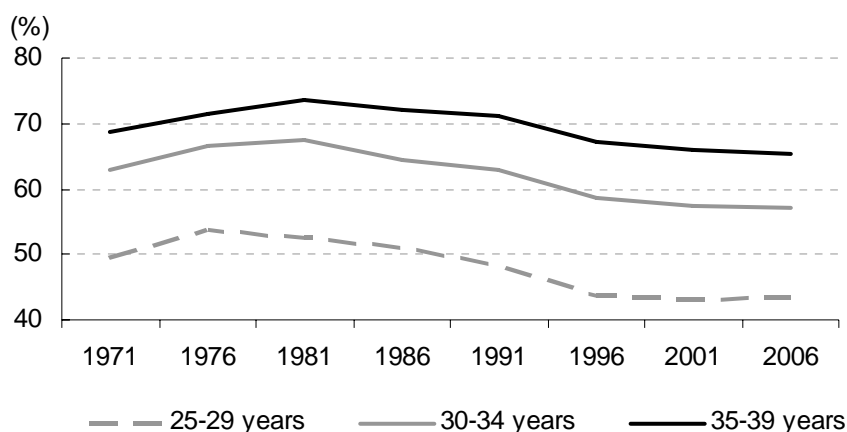
The paper concludes that the changing nature of the Great Australian Dream has contributed to its downfall. To redress the balance in relation to housing, what is needed is a return to those aspects of the Great Australian Dream that were important when the concept first evolved: security and stability for those who seek it. This can only be achieved by giving up the speculative wealth accumulation and tax-advantaged unearned gains that became important by default as a result of economic circumstances in the 1970s, and that transformed the Great Australian Dream into the Great Australian Nightmare in the 1990s. It need not mean giving up the dream of home ownership.

# 1 THE CHANGING DREAM

Over the past few years, housing affordability has regularly dominated the headlines, initially as rising house prices pushed access to home ownership out of reach and, subsequently, as increases in interest rates created repayment problems for those who had taken on significant amounts of housing debt. Most media attention is focused on the affordability problems faced by aspiring first home buyers, who are seen to be giving up the Great Australian Dream. The data in Figure 1 suggest there is considerable evidence to indicate that they are giving up that dream.

Figure 1 shows a steady decline in age-specific home ownership rates for younger households from the mid- to late 1970s. Between 1976 and 2001, home ownership rates for those in the 25–29 year old age group declined by 11 percentage points (from 54 per cent to 43 per cent), by 10 percentage points (from 67 per cent to 57 per cent) for those in the 30–34 year old age group and by 6 percentage points (from 72 per cent to 66 per cent) for those in the 35–39 year old age group.

**Figure 1: Home ownership rates over time for younger households by age cohort**



Source: special request tabulations, ABS censuses

This paper examines the implications for young adults of the changing patterns of investment in housing over several generations. It provides a brief snapshot of three distinct phases in the evolution of home ownership: as an aspiration of households in the 1950s and 1960s, as a driver of inequality for their baby boomer children in the 1970s and 1980s, and as a fading dream of their grandchildren from the 1990s to the present. Whilst it might be dangerous to use the past to predict the future, it is equally dangerous to ignore the lessons of the past in determining what might happen in the future.

Badcock and Beer (2000) describe those who entered home ownership in the 1950s and 1960s as the Safe and Sound generation and those who entered in the 1970s and 1980s as the pampered generation. As will be argued below, it is the baby boomer generation that profited most from home ownership. The question of whether their Generation X children<sup>1</sup> – described by Hugh Mackay as the Options generation (Mackay, 1997) – can or will enter home ownership has yet to be answered.

<sup>1</sup> A common convention is to define the baby boomer generation as those born between 1946 and 1964. This overlaps marginally with that of Generation X, defined as those born between 1961 and 1981.



The three sections of this chapter are based on the experiences of these three generations. The chapter begins with the rise of home ownership in the period immediately following WWII, and ends with the rise in rental investment that dominated the most recent house price boom. It describes how the changing economic and social climate changed the nature of the Great Australian Dream for each of these generations, and suggests that this has contributed to its downfall. Chapters two and three highlight implications of the changes that have occurred and suggest some changes that might be needed for the home ownership dream of the past to be re-imagined for the future.

## 1.1 The 1950s and 1960s dream

In the 1950s, the popular portrayal of the Great Australian Dream was of a modest three-bedroom home on a large block of land, popularly described as a quarter acre block – although it most probably only reached those proportions in relatively few locations. By the 2000s, this same image had come to portray a conservative vision of Australia. With its suburban picket fence, and its evocation of, and inseparable association with, the image of a nuclear family comprising a single male breadwinner and 2.3 children, the vision is as dated as the statistics it embodies.

At the end of the 1950s, the median house price was around \$7,000–\$8,000 at a time when average earnings were around \$2,000 per year. At the interest rates of the time (of around 5 per cent), such an income would support a loan of more than \$9,000. In other words, the house price to income ratio was around 3-4 and there was effectively no so-called deposit gap. A significant contribution to the expansion of home ownership came from houses built under the Commonwealth State Housing Agreement of the time – in other words, from social investment. These houses were on-sold on the basis of a 5 pound (\$10) deposit and funded through mortgage finance provided by a highly regulated mortgage finance industry or by direct government lending. By the mid-1960s, one-third of housing loans outstanding were provided by direct government lending, through war service loans and state-based schemes (Milligan, 2003).

The nuclear family was the dominant household form and a single male breadwinner was the norm. Strong economic growth, a stable economy, high minimum wages as a result of a centralised wage fixing system, and certainty and optimism gave households the confidence to undertake a long-term mortgage commitment.<sup>2</sup> In the 1950s, the home ownership rate increased from just above 50 per cent at the start of the decade to above its current value of around 70 per cent at the end of the decade. Housing careers were clearly defined. Young people married and partnered at the same time, had their first child and then entered home ownership (Winter and Stone, 1999). Home ownership provided shelter, security and a stable and affordable environment in which to raise a family. The private rental market served as a temporary tenure for the young.

The dream of home ownership in the 1950s and 1960s, therefore, might be seen as a fairly modest dream. It was a dream of shelter, security and stability and was made possible by affordable housing.<sup>3</sup>

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<sup>2</sup> Good background material can be found in Badcock (2000) and Milligan (2003).

<sup>3</sup> Troy (2000, p718) implies that the support for home ownership by the Menzies government might more accurately be regarded as a policy initiative to create a "patriotic, co-operative and cohesive society - one which agreed with Menzies' view of the world, that is: he wanted a docile, compliant society."

## 1.2 The 1970s and 1980s dream

By the 1970s, as the baby boomer generation started to come of age, the clear patterns from the 1950s started to blur. There were a number of very significant changes, both social and economic. Social change arose as women stayed in the workforce longer before starting their families. This contributed to the phenomenon of the two-income household. Changes in family law resulted in increased separation and divorce. This added to an increased proportion of single-parent families and single-earner households. The economic certainty and stability associated with the steady economic growth, low unemployment and low inflation of the 1950s and 1960s was shattered by a slowdown in economic growth and the simultaneous onset of both high unemployment and high inflation. The latter created pressures on mortgage markets, which initially squeezed the amount of funds available for lending for housing, and ultimately contributed to the removal of the regulations that had kept housing interest rates relatively low.

One of the effects of these changes was that access to housing became more difficult. House prices remained around 3–4 times the average annual earnings of a single male, but the onset of inflation meant that the deposit gap grew rapidly, primarily as a result of the increase in interest rates associated with higher inflation. By the mid-1970s, median house prices had increased to just over \$32,000 and average earnings had increased to just over \$8,000. At the then current interest rates (of close to 10 per cent), this income level could support a loan of less than \$25,000. This left a deposit gap roughly equal to annual average earnings and a resultant requirement on the household to save the equivalent of one year's income before the loan they could support with their income, combined with their deposit, would be sufficient for them to purchase a median-priced dwelling.<sup>4</sup>

By the mid-1980s, whilst access to home ownership was becoming more difficult, the introduction of a capital gains tax that exempted owner-occupied housing also made it more desirable. For those who could access it, home ownership became a tax-advantaged hedge against rampant inflation.<sup>5</sup> The emergence of a very significant deposit gap, however, meant that households with even moderate incomes and with no savings capacity were excluded from home ownership. Home ownership was no longer affordable for all.

Under such circumstances, the Great Australian Dream became a dream of more than shelter, stability and security. It became a dream of an investment opportunity – and a driver of inequality. The need to save for a deposit from the mid-1970s (assisted for many, but obviously not all, by the transition to a two-income household) could be seen as initiating what has since become an obsession with the role of home ownership in contributing to wealth accumulation. In this process, housing also became a status symbol, with increasing aspirations (supported by the greater spending power of two-income households) leading to ever-increasing housing standards, as reflected in today's McMansions<sup>6</sup>.

However, it is important not to romanticise the past or demonise the present. The increases in housing standards that have occurred in the past 50 years are probably way beyond the capacity of earlier generations to even imagine. Despite this, while

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<sup>4</sup> These outcomes can be seen in Figure 2 and Figure 3 in the following section.

<sup>5</sup> From the early 1970s to the early 1980s, the average annual inflation rate exceeded 11 per cent. It peaked at almost 17 per cent in 1975. Interest rates, which were regulated during the 1970s and deregulated in the early 1980s, reached the same peak in the late 1980s.

<sup>6</sup> In the Treasurer's view, this is an inappropriately derogatory term (Costello, 2006).

rising housing standards and the continued urban sprawl associated with a suburban lifestyle are likely to contribute to future environmental sustainability problems, they are not the prime cause of affordability problems. Two far more important factors can be identified. These are, first, the scarcity of land brought about by the demands of an increasing population and, secondly, how this valuable resource is shared among the population.

The accumulation of personal wealth that has come to be associated with home ownership does not come from the dwelling that provides shelter; it comes from the land on which the dwelling is located. In Hugh Stretton's words, land becomes

"a double unequalizer. As economic growth stimulates demand for accessible urban land... its unequal ownership further unequalises wealth and income. There are the direct transfers via rents and prices to inheritors and investors in land, and indirect transfers from those who don't own land and houses to those who do." (Stretton, 1976, p. 217).

A government report of the day highlighted the indirect transfers that arise from renters to home owners (Priorities Review Staff, 1975). Essentially these are due to the fact that, for home owners, the income and wealth generated by the ownership of land is not taxed. When inflation – specifically, dwelling price inflation – is high, the value of untaxed and unearned capital gains can be significant.

The inequities arising from differential access to what effectively has been the major form of wealth accumulation available to Australian households are exacerbated by strong spatial differences in the extent of land price inflation, particularly in urban areas. That this would happen was recognised at the time by Whitlam in his 1972 policy speech:

"Whatever benefits employees may secure through negotiation or arbitration will be immediately eroded by the costs of living in their cities; no amount of wealth redistribution through higher wages or lower taxes can really offset the inequalities imposed by the physical nature of cities."<sup>7</sup>

The physical nature of Australia's cities highlights two key disadvantages in relation to the country's settlement pattern. The first is that Australia has too few major cities. There is possibly no other country in the world that has over 60 per cent of its households in just six state capitals and almost 40 per cent in just two of those – Sydney and Melbourne<sup>8</sup>. Outside the capital cities, there are only a few major urban areas with more than 100,000 households. The scarcity of water is one obvious explanation for why this pattern has changed little in the time since Federation.

The second disadvantage is that Australia's major population growth occurred well after the arrival of motorised transport. This resulted in an undue reliance on road transport and a sprawled urban form that worked reasonably well when the cities were little more than large country towns with no congestion, ready access to most facilities and a relatively flat land price gradient. It has become problematic as cities have grown and as increasing demands on existing infrastructure have reduced access to employment opportunities and recreational facilities and have increased land price gradients.

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<sup>7</sup> As quoted in Badcock, B. (1984)

<sup>8</sup> This point has been made by researchers at the Reserve Bank (Ellis and Andrews, 2001). They also suggest that Australia's federal structure has contributed, with the state capitals acting as 'primate cities dominating the surrounding regions'.

The scarcity of land is a contributing factor to affordability problems about which relatively little can be done. Urban consolidation, by reducing the amount of land needed for each dwelling, takes some of the pressure off the limited supply of land available in urban areas. Land release at the fringe takes some more of the pressure off, although the benefits are offset by charging for infrastructure costs rather than spreading the costs of these over the whole community. Improved transport policies relieve the pressure on centrally located land within urban areas. Regional development policies take some pressure off urban areas.

With the existing settlement pattern in Australia, however, these policies do little to reduce inequities that arise from pressures on land prices, and the increasing land price gradients that have arisen in urban areas as the population continues to grow and as standards of living continue to increase (Ellis, 2006; Kohler and Smith, 2005; Productivity Commission, 2004). These inequities arise because increases in the value of land are not seen as a common resource to be shared by all. They are expropriated by those fortunate enough to own land at the times when its value increases.

### **1.3 The 1990s and 2000s nightmare**

The inevitable and unremitting pressures generated by real increases in land values has meant the dream of security and stability from the 1950s and the dream of wealth accumulation from the 1970s have become a nightmare for the most recent generation of aspiring home purchasers.<sup>9</sup> Some of the early signs of the transition from dream to nightmare arose with the uncertainties created by a no longer predictable economic environment and especially with the 1980s impact of rapidly rising interest rates on the ability of those who had borrowed up to, and possibly beyond, their capacity to sustain repayments on their mortgages.

Despite the decline in interest rates from the dizzy heights reached at the end of the 1980s, the 1990s and 2000s generation of first home buyers face even greater affordability problems than their parents faced a generation earlier. Rather than making housing more affordable, the decade-long downward trend in interest rates from 1990 to 2000 resulted in a borrowing frenzy and an unprecedented increase in household debt.<sup>10</sup> This, along with a number of unfortunately timed incentives such as the change in the capital gains tax regime in 1999<sup>11</sup> and the introduction of the First Home Owners Grant in 2000, created upward pressure on house prices from both investors and owner-occupiers alike so that, for the first time, the house price to income ratio rose dramatically, as can be seen in Figure 2.

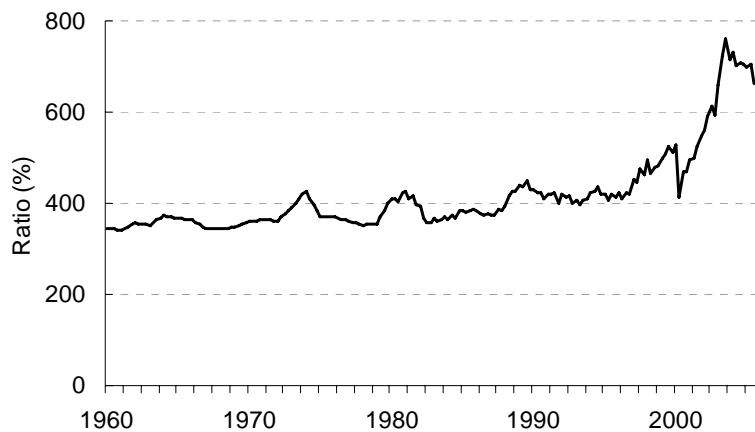
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<sup>9</sup> It is overly simplistic to portray only the current generation as facing what Kemeny, in his seminal critique of home ownership, called the great Australian nightmare as far back as 1983 (Kemeny, 1983). The uncertain economic and changing social environment of the 1970s and the rapid rise in interest rates in the 1980s meant many households who used mortgage finance to purchase their own homes during these decades faced significant problems after they entered home ownership.

<sup>10</sup> During the 1990s, interest rates fell from their peak of 17 per cent to between 6 and 8 per cent, where they have remained until the present (2007). Despite their dramatic decline, current rates are still several percentage points higher than the housing loan rates of 4 to 5 per cent dominant in the 1950s and 1960s.

<sup>11</sup> From a tax on real, realised capital gains at the owner's marginal tax rate to a tax on actual capital gains upon realisation at 50 per cent of the owner's marginal tax rate (with transition arrangements). In both cases, capital gains from owner-occupied housing have been exempt.

**Figure 2: House price to income ratio**

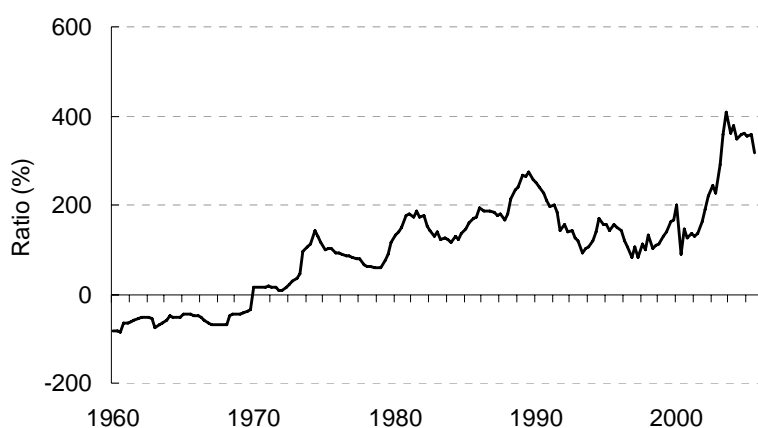


Source: Author's estimates. House price data from 1986 are median established house prices for Australia as reported in the HIA-Commonwealth Bank Housing Reports (provided by HIA). Prior to 1986, they are based on median established house prices for Melbourne from BIS Shrapnel data (provided by the Department of Industry Technology and Commerce). From 1983, income data are based on annual equivalents of Average Weekly Ordinary Time Earnings (full time male) (ABS 6302.0 Table 3). Prior to 1971 based on Average Weekly Earnings (full time male) (RBA Occasional Paper No. 8, Australian Economic Statistics 1949-50 to 1989-90); from June 1971 to June 1983 derived from national accounts data (RBA Table G06). Data prior to 1971 are annual averages of male earnings of quarterly estimates for financial years; post 1971 are June quarter data. Similar charts for a shorter time span can be found in RBA (2006 ) and in Demographia (2007)

Much of the increase in house prices between 2000 and 2003 has been attributed to a boom in investor demand, stimulated both by the interaction of taxation and house price inflation making investment in housing tax-effective and by supply-side developments that have made investor finance both cheaper and more readily available (RBA, 2002).

In the past few years, much has been made of the doubling of the house price to income ratio from its long-run historical average and the consequent rise in the household debt to income ratio (for example, Macfarlane, 2003). However, because much of this increase has been associated with a significant decline in interest rates, it is not the increase in the house price to income ratio that makes housing unaffordable. What has made housing even less affordable now than in the past is the increase in the deposit gap. After some signs of recovery with the decline in interest rates in the mid-1990s, the deposit gap to income ratio is now 3 to 4 times greater than it was in the 1970s, when affordability problems started to emerge. This can be seen in Figure 3 (which also shows the considerable volatility in this ratio and highlights the importance of taking a longer-term rather than a shorter-term view of affordability trends).

**Figure 3: Deposit gap to income ratio**



Source: Author's estimates. House price and income data as in Figure 2. Deposit gap derived from borrowing capacity defined by a 30 per cent repayment to income ratio and a 25 year standard variable rate housing loan. Interest rates: From 1960, interest rates taken as standard variable rate housing loan at June (RBA , Table F05); prior to 1960 predominant housing loan rate over calendar year (RBA OP 8A, Table 3.21)

Households and lending institutions have responded, respectively, by taking out or by providing larger and/or less secure loans. According to the mortgage calculator provided by one prominent mainstream lender, a two-earner couple equally contributing to a combined household income total equal to average earnings could borrow to a point where repayments accounted for almost 40 per cent of their gross household income.<sup>12</sup> The answer to the question of what happens to their repayment capacity if they have children most probably explains why an increasing proportion of them have not yet begun to procreate. Financial liberalisation also has resulted in an increase in low-doc loans and sub-prime or non-conforming loans, both of which are inherently more risky and likely to be more expensive than mainstream loans.<sup>13</sup>

Two additional factors in today's economic environment add to the problems faced by households who undertake these huge repayment burdens. In the first place, these borrowers no longer have the inbuilt protection that inflation provided when rising deposit gaps and a regulated financial system first pushed borrowers into expensive cocktails of first and second mortgages in response to the emerging affordability problems of the 1970s. In the 1970s, the combination of flat repayment schedules over the life of a loan and an inflation-driven earnings growth of 10 to 20 per cent per annum meant repayments that started at 30 per cent or more of household income declined to 15 per cent in just 5 years or so. Today, with a lower inflation-driven growth in earnings, the same reduction in the burden of repayments to income occurs only after more than 10 years.<sup>14</sup>

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<sup>12</sup> This estimate is based on the assumption of no children, a 25-year loan, an interest rate of 8 per cent and no outstanding personal debts. See Yates (2006) for more detail. Similar calculations for a single person on a similar income put the implied debt servicing ratio at nearly 50 per cent (RBA, 2005a, Box D).

<sup>13</sup> Low-doc loans are loans for which borrowers self-verify their income. The RBA (2005b, box B) reports an arrears rate for securitised low-doc loans three times higher than for conventional loans. Similar concerns about the additional risks imposed by lending to relatively risky borrowers can be found in the international literature. See, for example, Munro et al. (2005) for the UK.

<sup>14</sup> These examples both assume constant real incomes for the life of the loan.

A second problem is potentially even more insidious. It arises from the increased insecurity that stems from labour market changes that have taken place in the past few years, with structural change workforce reforms leading to a greater role for low-paid, part-time and casual employment. These changes potentially make it more difficult or more expensive for marginal purchasers to commit to a long-term mortgage. ASIC reports that “low doc loans have been aggressively marketed in some cases, to people with a troubled credit history, casual workers or self-employed people who may be in a weaker position when it comes to dealing with the financial risks involved” (ASIC, 2007).

## 2 IMPLICATIONS

The impact of these changes and the decline in home ownership rate of the first wave of Generation X households was shown in the age-specific home ownership rates in Figure 1. A number of commentators have been sanguine about this decline, arguing that it reflects a lifestyle choice or simply a deferral of home ownership.<sup>15</sup> Under the combined present circumstances – of historically high housing unaffordability, increased labour market flexibility potentially creating increased uncertainty about future incomes, and the fact that the only existing affordable housing is likely to be located far from the centres of the growth engines of the economy – it is not at all surprising that home ownership rates among the young have declined dramatically. It is still an open question as to whether this decline is temporary or permanent. If, however, age-specific home ownership rates among the young are to return to the peaks reached when the baby boomers were entering the housing market, the downward trend observed in these rates will need to be reversed.

Even if the relationship between house prices and household incomes returns to the levels of the time when the baby boomers entered home ownership, there will be a significant deposit gap that Generation X households will need to bridge before they can access home ownership. On current lending criteria with maximum permissible debt servicing ratios, a household with an income of around \$50,000 (roughly equal to average weekly earnings) could borrow just over \$200,000 (with repayments at close to 40 per cent of its income)<sup>16</sup>. On the basis of the June 2005 median house prices in Australia of just under \$350,000<sup>17</sup>, this implies a savings requirement of three times the household's annual income.<sup>18</sup> Median house prices would need to be at least \$100,000 lower for Generation X to have to accumulate no more than the same deposit in relation to income as their parents. Median house prices would need to be more than \$150,000 lower if Generation X (and, following them, Generation Y) are to have the same access to home ownership as their grandparents.

The size of the current deposit gap means the current generation of potential home buyers are likely to become owner-occupiers only if they obtain a significant amount of assistance with their deposits. The most likely source of this is their parents or grandparents, whose real wealth has increased significantly, primarily as a result of house price inflation. Figure 4 illustrates increases in real net wealth per capita since 1960 and highlights the role that housing has played in total real wealth. It shows a pattern of relative stability throughout the 1960s, when the Safe and Sound generation became home owners, and through to the 1970s and 1980s, when the baby boomers were first home buyers.

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<sup>15</sup> Examples can be found in Baxter and McDonald (2004) and Mudd, Habtemarian and Bray (2001). Baxter and McDonald identify delayed marriage and fertility as the primary driver of the decline in home purchase.

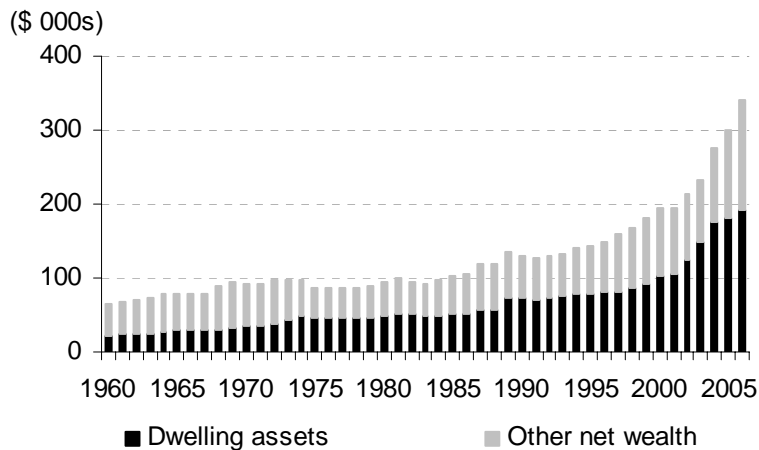
<sup>16</sup> This is based on a 25-year loan at an interest rate of 8.07 per cent.

<sup>17</sup> Median for Australia based on weighted average of ABS data for capital cities (ABS (2005) *House Price indexes: Eight Capital Cities* Cat.no 6416.0 Tables 7 and 8).

<sup>18</sup> In principle, the First Home Owner's Grant reduces some of this pressure, but this benefit is offset by transaction costs associated with home purchase.



**Figure 4: Real private sector wealth per head (\$2003/04)**

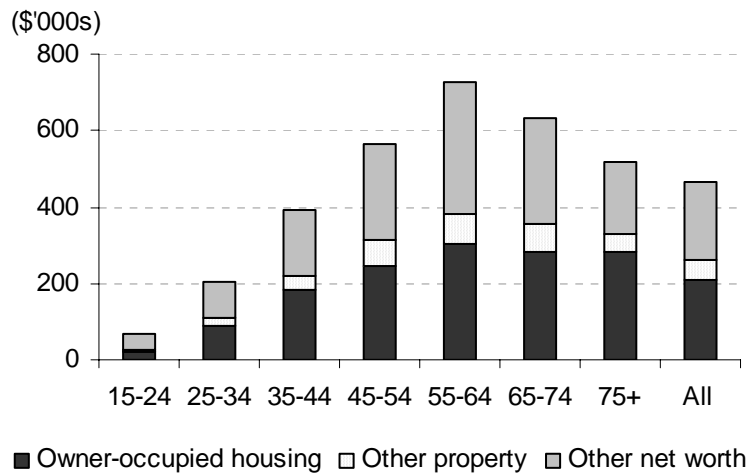


Source: Treasury (2007)

It also shows the rapid increases in per capita net wealth that occurred as the baby boomers became established during the 1990s and 2000s. Per capita real wealth increased by less than a third in the 20 years from 1965 to 1985. It increased almost threefold in the 20 years from 1985 to 2005. It is during this period that direct social investment in housing began its downward slide (Productivity Commission, ROGS, various years), consistent with a generally greater reliance on the market to provide goods and services in Western democracies.

A critical factor in whether Generation X will be able to benefit from this accumulation of wealth is who has, and what happens to, baby boomer wealth. Figure 5 shows that the greatest per household share of this net wealth is owned by Generation X's baby boomer parents, currently aged between 40 and 60, followed closely by their grandparents, now at or beyond retirement age. Much of this pattern of wealth ownership, of course, simply reflects a natural progression through the life cycle. Figure 5 also shows that it is older, rather than younger, households who hold the greatest amount of wealth in investment housing. Kohler and Rossiter (2005) show that the propensity to own residential property other than owner-occupied property is strongly influenced by age and increases with income and wealth, with the marginal impact of income being even greater for investment property than for owner-occupied property.

**Figure 5: Household net worth by age of reference person, 2003/04**

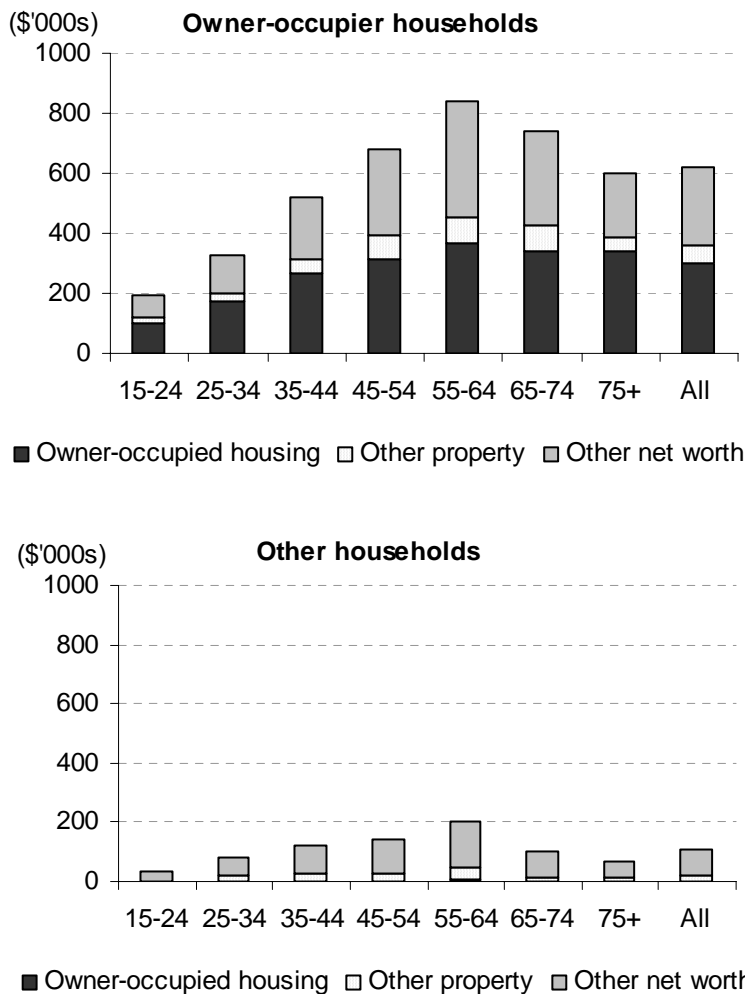


Source: ABS Cat. No. 6554.0, 2003-04, Table 20

For those whose parents are home owners (or investors in housing), assistance will be feasible if their parents are willing to pass on some of their accumulated wealth rather than choosing to spend it or being forced to do so by retirement income policies.

A form of wealth transfer that relies on redistribution within the family is inequitable for several important reasons. In the first instance, only those brought up with the security that home ownership generally provides are likely to be able to benefit. Figure 6 disaggregates the data presented in Figure 5 according to whether or not the household is an owner-occupier. The results suggest a clear correlation between net wealth derived from home ownership and total net wealth. In every age group, home owners not only have greater average net housing wealth but also have significantly greater average non-housing wealth.

**Figure 6: Household net worth by age of reference person and tenure, 2003/04**



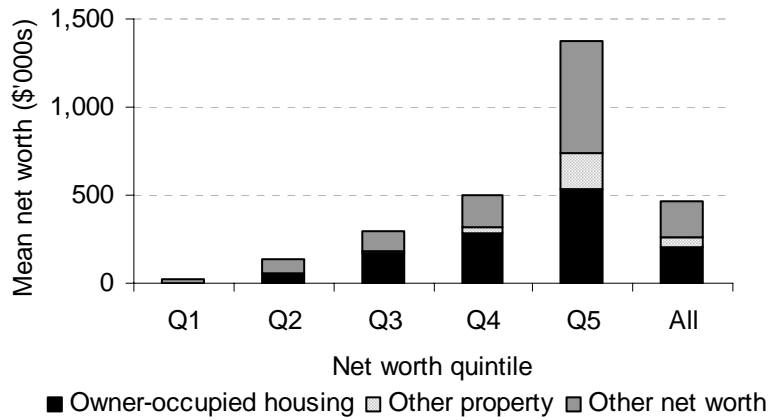
Source: confidentialised unit record file, ABS Survey of Income and Housing 2003-04

The results in Figure 6 also show that parents or grandparents who did not achieve home ownership are unlikely to be able to provide Generation X with adequate assistance even if they wished to do so. Only if non-owner-occupier grandparents transferred all their net worth to their grandchildren, or non-owner-occupier parents transferred more than half their total net worth to their children, would there be a sufficient intergenerational wealth transfer to bridge the current deposit gap for Generation X households with incomes at least equivalent to average earnings. For Generation X households with incomes below average earnings, even greater levels of assistance are required. This suggests that, far from being the great equaliser of wealth, as it was seen to be in the past, owner-occupied housing now has the capacity to add to economic inequality by reinforcing existing inequalities of wealth from one generation to the next.

A second reason why wealth transfer that relies on redistribution within the family is grossly inequitable can be seen in the results presented in Figure 7, which shows the distribution of household wealth in Australia in 2003/04. In 2003/04, households in the top wealth quintile owned 50 per cent of total equity in housing in Australia (and 58 per cent of total net worth). Households who first had the opportunity to enter the

housing market in the heady days of the 1970s, and who are now aged 55–64, have the greatest per household share of this wealth.

**Figure 7: Household net worth by net worth quintile, 2003/04**



Source: confidentialised unit record file, ABS Survey of Income and Housing 2003-04

A third reason why intergenerational transfers are likely to be inequitable is that, as has been argued regarding government-provided assistance with deposits, they can be counterproductive in that they contribute to increased demand for housing and add fuel to the house price fire. This can aggravate problems of access for those currently unable to bridge the deposit gap and unable to benefit from family wealth.

Relying on private transfers within the family as a solution to the problems of affordability will not address the inequality that is embedded in the current system of housing provision. A more equitable way is needed of distributing and redistributing the unearned increases in wealth that, in considerable part, are generated from land ownership.

The next section of this paper examines a way of moving towards a housing system that is fairer for all.

## **3 FAIRNESS AND HOUSING**

### **3.1 Defining a fair housing system**

The right to adequate housing is enshrined in Article 25 of the United Nations Universal Declaration of Human Rights. This rights-based definition suggests that a fair housing system is one that ensures an adequate supply of dwellings for all households within their capacity to pay. As an ever-increasing number of households in Australia face unaffordable housing costs (over 1 million households in 2003 paid at least 30 per cent of their household income in meeting their housing costs), it is questionable whether the current system of housing meets this minimum criterion. For the unacceptably high number of people who are homeless in Australia (close to 100,000 in 2001), it is clear that it does not.<sup>19</sup>

Housing is not a simple commodity that can be divided up and allocated equally to all. It is a complex good providing shelter (for all but the homeless), access to a wide range of amenities (that are valued differently by different people) and the main means of accumulating wealth (for the shrinking number fortunate enough to own housing in an area where rising house prices increase the value of their investment over time).

While not every household in Australia aspires to a mansion overlooking Sydney Harbour, the obvious reality that, if they did, they would not all be able to achieve their aspiration, is a clear example of the problem of determining what constitutes fairness in housing. Access to most housing is governed by willingness and capacity to pay. Because all but 5 per cent of housing in Australia is provided by the market, the structure of ownership and control of housing reflects the inequalities of income and wealth that underpin a market-based economic system.

Markets, however, do not operate in a vacuum. One way of determining whether the housing system is fair without tackling the more fundamental question of whether the economic system generates a fair distribution of income and wealth, is to assess whether the taxes and subsidies that govern the housing market help to make the existing system fairer. While there is little possibility of having a fair housing system until the economic system that underpins it is fair, it is possible to have a housing assistance system that contributes to a fairer economic system by ensuring that existing inequalities in income and wealth are ameliorated rather than exacerbated.

### **3.2 Defining a fair housing assistance system**

The types of policies that would generate such a system are those that assist the most disadvantaged in our economic system. Such a system would provide no assistance for outright owners, except possibly for older asset-rich and income-poor households who need a fair means of extracting their housing wealth to maintain an adequate standard of living. It would not assist would-be purchasers to accumulate housing wealth. For renters it would ensure that income was sufficient to meet the costs of a minimum acceptable standard of housing and that there was an adequate supply of affordable housing. It would provide, or subsidise the provision of, affordable housing through whatever cost-effective means was available.

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<sup>19</sup> Data taken from Yates and Gabriel (2006) and Chamberlain and Mackenzie (2003).

### 3.3 The current housing assistance system

The explicit grants-based system of housing assistance to renters, with some anomalies, bears some resemblance to this ideal. Public or community housing and assistance to private renters is targeted to those most in need. However, publicly funded housing, which provides adequate and generally affordable housing for lower-income households, is under-resourced, often under-maintained and houses a declining proportion of households. The assistance provided to low-income private renters has improved significantly since its introduction and reduces the burden of housing costs. However, it is often inadequate and it is not available to all who need it. Both public housing and rent assistance serve to alleviate existing inequalities. Both pass the fairness test. First home purchasers receive generous grants to assist them into home ownership, but recipients are not required to repay these grants, and grants are not targeted to those most in need and are inadequate to bridge the deposit gap for lower-income households. It is less obvious that these grants pass the fairness test.

The most significant amount of housing assistance is not explicit but is provided to owner-occupiers through the tax system rather than through direct cash grants. Owner-occupied housing is exempt from capital gains tax, exempt from the assets test for pensions, exempt from land taxes and exempt from taxes on income-producing property. These exemptions result in owner-occupied housing being the most tax advantaged form of asset accumulation that remains after the tax reforms of the 1980s.<sup>20</sup> The timing of this assistance, however, is such that many receive the greatest benefit when they least need it. Young, low- or moderate-income purchasers receive virtually no indirect assistance. Older, higher-income households receive thousands of dollars worth of tax exemptions (Wang et al., 2004; Yates, 2003).

Policies that benefit home owners add to the demand for owner-occupied housing and for housing finance. In doing so, they add to the upward price pressures that push ownership out of the reach of low- to middle-income groups. Access to housing, housing costs and assistance for housing are all affected by inequalities in income and wealth. Inequalities in the support provided for housing add to the inequalities in access to home ownership and contribute to a cycle of housing-related disadvantage. Such policies fail the fairness test.

As indicated in Chapter 2, a more equitable way is needed of distributing and redistributing the unearned increases in wealth that, in considerable part, are generated from land ownership. Even partial removal of just some of the exemptions that favour home ownership at either federal or state level would be a good start.

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<sup>20</sup> Recent changes to superannuation policies means that, for older households at least, investment in superannuation now rivals investment in housing in terms of tax advantage. One concern this change raises is that the role of 'mums and dads' investors using rental investment as a de facto superannuation policy will decline and will be replaced by superannuation funds seeking a much greater rental return than hitherto has been achieved. Under such a scenario, households who cannot gain access to owner-occupation are likely to face even greater affordability problems in the future.

## 4 CONCLUDING REMARKS

Has the Great Australian Dream ended? Affordability problems and lack of access to housing in general, and owner-occupied housing in particular, are essentially problems of income and wealth distribution. They can be reduced only if they are tackled as such. If the unearned capital gains generated by population growth and by economic growth are captured by the wealthiest households in the population and by those who, by virtue of little more than their age, are current owners of one of the scarcest factors of production in our economy – well-located land – then the only members of future generations who will not have an affordability problem are some of the children of the most favoured generation Australia is likely ever to have.

To redress the balance in relation to housing, what is needed is a return to those aspects of the great Australian dream that were important when the concept first evolved: security and stability for those who seek it. This can only be achieved by giving up the speculative wealth accumulation and tax-advantaged unearned gains that became important by default as a result of economic circumstances in the 1970s and that transformed the Great Australian Dream into the Great Australian Nightmare in the 1990s. It need not mean giving up the dream of home ownership. It may mean changing what it entails.

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