

Paying the price for easy credit

Comment

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The housing affordability debate has become badly muddled, and there's a growing risk of good intentions lurching on to bad policy.

Most Australians accept we have an affordability crisis. But why? Before we do anything, we've got to be clear about exactly what type of problem exists.

Indeed, many of today's alleged affordability problems are not really problems at all, but rather reflect the benefits of sustained economic growth and biased measures of housing stress.

The most widely used measure of "housing affordability" is total household home mortgage interest payments as a percentage of nationwide household disposable income. As the Reserve Bank of Australia has noted in recent commentaries, these interest payments have lifted to almost 12 per cent of household income, compared with around 7 per cent in the 1990s.

And interest payments are now higher than when Paul Keating had 18 per cent mortgage interest rates in the late 1980s.

So far so bad. But does this necessarily mean households are worse off and struggling to make payments? Far from it.

As RBA analysis makes clear, a good chunk of the rise in interest payments in recent years has come

HOME WORK

Proposals to make housing cheaper

- **Howard government:** Audit of federal government land holdings and states to release more land.
- **Federal Labor:** Tax incentives for home-deposit savers, capital grants and loans to non-government social housing providers, low-income housing tax credits, and reform of first-home owners' grants.
- **State housing ministers:** Shared-equity loans, more public housing and reform of federal rent assistance.
- **Housing Industry Association:** Double \$7000 first-home owners' grant, home loan savings accounts, depreciation allowances, residential infrastructure fund and share equity loans.
- **National Affordable Housing Summit:** Incentives for investment, capital grants to increase supply of social housing and government investment in residential infrastructure.
- **Australians for Affordable Housing:** More public housing, rental incentives, reform of tax incentives, shared equity schemes, income insurance for marginal home purchasers and better use of government land.

from more households taking on investment properties, or trading up to larger homes. These have typically been older and wealthier households who can easily handle higher debt.

And they've reacted to two positive developments in the economy. First, the trend decline in interest rates made it more affordable and advantageous to leverage further into housing assets.

Second, in economists' parlance, housing demand is a "superior" good — meaning households demand more of it as their incomes rise. With a solid economy and falling unemployment, many households are likely to have decided to spend relatively more of

their budgets on housing services. The average size and quality of the housing stock has improved notably in the past decade.

Another measure of housing affordability — specifically for first-home buyers — is the percentage of average household income needed to devote to servicing a mortgage on the median-priced home. This servicing burden has also increased considerably. But so what?

With a solid economy and an easing in credit standards, even first-home buyers are likely to have become more willing and able to spend up on homes.

It's no surprise, therefore, many are spending more of their household budgets on housing services, as

many were previously unemployed and/or credit rationed out of the market. First-home owner irritation has merely switched from not being able to get a loan to paying so much for one.

Meanwhile, the evidence suggests many of the alleged causes of Australia's housing "problem" — tax concessions, poor transport, land release and government charges — may have had only marginal effects. Australia's overall tax concessions for housing appear no worse than in other countries.

By international standards, Australian housing costs seem high, but largely because our relatively small population to land mass encourages us to clump together in a few highly urbanised centres, where housing space is usually at a premium. Urbanisation also has its advantages: if it didn't, more of us would live in cheaper country towns.

At the end of the day, housing is a market like any other — costs will reflect what households are prepared to pay.

A strong economy, lower interest rates and easier credit standards have increased our willingness and capacity to pay for such highly-priced services.

But we're also willingly paying more for our (flat-screen) TVs — yet who suggests this is an affordability problem that required government intervention?