

Submission to

SENATE SELECT COMMITTEE ON HOUSING AFFORDABILITY

by

Professor Robert Stimson and Dr Alistair Robson

UQ Social Research Centre, Institute for Social Science Research

University of Queensland

14 April, 2008

Housing affordability has become a matter of elevated concern recently, as evidenced by this senate select committee. This is more so for purchases of housing, but it is also true for renting. The overview I present here is a summary of the key material available, and as such covers only some pertinent and important aspects of housing affordability.

There has always been some element of housing affordability in Australia. People from lower socio-economic backgrounds are often excluded from either purchasing housing or renting. Those that are excluded from both options either share accommodation with family or friends, or are homeless.

Nor, are housing affordability issues evident solely in Australia. It appears evident that similar issues exist in many OECD nations (such as the USA and the UK). From reports in the media of falling house prices in the USA, we may hear less about housing affordability there in the coming months. A number of studies on housing affordability and house prices have found that Australian house prices are relatively high and unaffordable compared most other countries (such as the OECD and the *Demographia*¹ report). An OECD² report found that Australian house prices were over-valued in 2004 by 51.8 per cent, compared with 32.8 per cent for the UK.

¹ Demographia, "4th annual Demographia International Housing Affordability Survey"

The last time housing affordability held such an elevated level of national interest was in the late 1980's—prior to the previous recession—when interest rates rose to very high levels (as an example the official cash rate was between 17.0% and 17.5% on 23 January 1990³). It can be reasonable to propose during this period, housing affordability was low mainly because of relatively high interest rates. Comparatively, in the current episode of relatively low housing affordability it could be reasonable to propose that relatively high prices (and thus debt) are mainly the cause. Recent levels of interest rates are no-where near where the level of the late 1980's.

There are two major contemporary measures of housing affordability in Australia. One is produced by the Housing Industry Association and the Commonwealth Bank of Australia (HIA-CBA) and the other is produced by the Real Estate Institute of Australia (REIA). While both measures use different methodologies in calculating housing affordability, they both incorporate the major components of household income and the level of interest rates.

According to the HIA-CBA⁴ measure of housing affordability, the level of Housing Affordability in Australia in the December quarter of 2007 was at its lowest level since the series commenced in 1984.

REIA data is more difficult to access, as it costs money to examine. But based on media reports, the same broad patterns evident in the HIA-CBA measure appear to be showing in the REIA measures of housing affordability.

There are, however, some difficulties in the methodologies used in these indices to measure the incidence of housing affordability/unaffordability. The international benchmark measure of 'housing induced financial stress' it known as the 'Ontario measure', which is widely used internationally to determine the eligibility of a household for housing assistance. That benchmark figure is where a household in below the 40th percentile of the distribution of household income is incurring housing-related costs in excess of 39% of gross household income. That is indeed vastly different measure of housing financial stress than the ones being used in the indices that are popularly cited in the media. If that international benchmark figure is used, then the magnitude of the incidence of housing unaffordability changes significantly and its incidence is targeted more correctly to those households that really suffering housing-cost related income stress that is not likely to be related to other exogenous factors such as lifestyle choices and consumption preferences.

² OECD, OECD Economic Outlook, Issue 2, 2005

³ Reserve Bank of Australia, "Cash Rate Target", http://www.rba.gov.au/Statistics/cashrate_target.html, Accessed on 14/4/2008

⁴ Housing Industry Association, "Supply Measures will improve Affordability", 12/2/2008

Economic context

Given the economic context, it should not be a surprise that housing affordability is at low levels based on the housing affordability measures. The national economy has been performing well, with the national unemployment rate at very low levels (4.1% in seasonally adjusted terms compared with the 20-year average of 7.0%⁵), the level of chain volume GDP has been growing since 1991⁶, and incomes growth (as measured by wages and salaries - compensation of employees in current terms) has been strong (up 8.4% in 2007 compared with 6.3% in average annual terms over 20 years⁷). Australia has also benefited from historically high levels for its Terms of Trade (up 4.5% in 2007 compared with growth of 2.6% in average annual terms over the past 20 years⁸) which has resulted in strong growth of real gross domestic income (up 5.1% in 2007 compared with growth of 3.9% in average annual terms over the past 20 years⁹).

Such strong economic conditions mean relatively high incomes and increased confidence that jobs and income are secure. It is reasonable to assume that Households that are more confident in the stability of their income would be more likely to devote a higher share of the income to housing. This is because housing is considered by many economic commentators to be a superior good (which is where a larger proportion income will be spent on housing as incomes rises, i.e. the price elasticity of housing is greater than 1).

But these strong economic conditions have not been geographically even across Australia. The resource rich states (Western Australia and Queensland) recorded strong growth in real gross state product in recent years of 5.4% in 2006-07, which compares with annual average growth of 4.4% since 1989-90. Comparatively, real gross state product growth in the rest of Australia was much lower at 2.2% in 2006-07, lower than the 20-year annual average growth rate of 2.8%.

Strong growth in domestic final demand (up 5.2% in 2007¹⁰) compared with supply (GDP growth of 4.1% over the same period) has led to increased inflation in recent

⁵ Source: ABS, cat. no.: 6202.0.55.001 - Labour Force, Australia, Spreadsheets, Mar 2008, Table 02. Labour force status by Sex - Seasonally adjusted

⁶ Source: ABS, cat. no.: 5206.0 Australian National Accounts: National Income, Expenditure and Product, Table 1. Key National Accounts Aggregates

⁷ Source: ABS, cat. no.: 5206.0 Australian National Accounts: National Income, Expenditure and Product, Table 1. Key National Accounts Aggregates

⁸ Source: ABS, cat. no.: 5206.0 Australian National Accounts: National Income, Expenditure and Product, Table 1. Key National Accounts Aggregates

⁹ Source: ABS, cat. no.: 5206.0 Australian National Accounts: National Income, Expenditure and Product, Table 1. Key National Accounts Aggregates

¹⁰ Source: ABS, cat. no.: 5206.0 - Australian National Accounts: National Income, Expenditure and Product, Dec 2007, Table 2. Expenditure on Gross Domestic Product (GDP), Chain volume measures

years. The Reserve Bank of Australia's measures of underlying inflation (Weighted median Consumer Price Index and the Trimmed Mean Consumer Price Index) were at their highest levels in the December quarter 2007 since the series commenced in the June quarter 2003 (up 3.8% compared with a year earlier for the Weighted Median measure and 3.4% for the Trimmed Mean measure). As a result, the Reserve Bank of Australia has lifted the official cash rate to its highest level since 1992 (around 16 years ago)¹¹.

In summary, current economic conditions have led to strong growth in incomes and higher interest rates.

The price of housing is determined by the demand for and supply of housing. These shall now be explored in the following sections.

Demand for housing

The demand for housing is determined by household's willingness to use its income for housing purposes. With the economy performing well, strong incomes growth and low unemployment, it is reasonable to assume that households would be more willing to use more of their income for housing purposes.

According to the OECD¹², in relation to house prices:

"A combination of generalised low interest rates across OECD economies, coupled with the development of new and innovative financial products, have no doubt played an important role"

And particularly for Australia:

"In Australia, increased competition among credit providers has contributed to the doubling of the number of products provided by lenders."

The primary means that a household has to purchase a home, particularly for First Home Buyers, is borrowing. Nowadays, home buyers can borrow from both banks and non-bank financial institutions. There have been numerous financial innovations over the past 20 years, too many to mention here. But, it appears to be commonly accepted among economists that such financial innovation has led to the ability for borrowers to increase the amount they may borrow. According to the OECD¹³, some examples of this financial innovation in Australia include the deposit

¹¹ Source: Reserve Bank of Australia - http://www.rba.gov.au/Statistics/cashrate_target.html, Accessed on Sunday 13/April/2008

¹² OECD, OECD Economic Outlook, Issue 2, 2005

¹³ OECD, OECD Economic Outlook, Issue 2, 2005, p.139

bonds, split purpose loans, non conforming loans, etc. The Reserve Bank of Australia has also commented that credit standards have eased in recent years¹⁴. This would have increased the amount of borrowing available for housing.

There are other factors that affect the demand for housing, such as demographic. Recently, Australia has experienced relatively high immigration, and there has been the ongoing aging of the population and lower household size. According to the Australian Bureau of Statistics¹⁵, net overseas migration into Australia in the year to the September quarter 2007 was 179,100 people – its highest level since the current series began in the June quarter 1981. In the year to the September quarter 2007, most of these people settled in New South Wales (53,488) and Victoria (48,222).

Saul Eslake, Chief economist of the ANZ Bank, also concurs that relatively low interest rates contributed to high price growth¹⁶. He also suggests that the Federal governments cut to capital gains tax in 1999 as another key driver, which made negative gearing more attractive.

The geographic distribution of demand for housing is quite diverse. This is particularly so for large cities, as Rory Robertson of Macquarie Bank points out:

“There’s this never satisfying compromise between proximity, being close to the action and the size of houses and yards and as our cities get bigger, literally, there’s less room for everyone to be living in nice houses with big yards”¹⁷

As Rory Robertson points out¹⁸, cities/towns and suburbs in cities which face relatively high house prices tend to be either close to the CBD or along the coast of Australia. In these areas, it is not easy to match the high demand for housing with more supply of land. Thus, low housing affordability is geographically concentrated because simply these areas are where people prefer to live.

This compares with Alan Moran’s view (Institute of Public Affairs), based on his interpretation of the International *Demographia* reports on International Housing Affordability in English speaking countries that demand is less of an influence on houses prices than the lack of supply due to government planning regulations and charges.

¹⁴ Reserve Bank of Australia, “Financial Stability Review”, Household and Business Balance Sheets, March 2008

¹⁵ ABS, cat. no.: 3101.0 - Australian Demographic Statistics, Sep 2007, Table 1. Population Change, Summary - Australia ('000)

⁵ Schneiders, B. and Millar, R., “Australian dream just a recession away”, The Age, 17/2/2007

¹⁷ Bevan, S., “Home Ownership a distant dream for many”, The 7.30 report, Australian Broadcasting Corporation, Broadcast on 6/2/2007 – <http://www.abc.net.au/7.30/content/2007/s1841718.htm>

¹⁸ Irvine, J., “Sydney not alone in seeking housing crisis solution”, Sydney Morning Herald, August 25, 2007

Supply of housing

In a perfectly competitive market - which is rarely the case in reality - the quantity of houses and apartments supplied will increase in response to higher prices over the long run (assuming that there is a price elasticity of supply for housing which is positively sloped and that there is land available with no government restrictions). In the short run however, houses and apartment cannot be built quickly. This means that when demand for housing rises when there are strong economic conditions, supply can often not catch up in the short term.

State and local governments have most of the power in determining the supply of new housing. This is done through mainly zoning and planning rules. For housing built on the fringes of capital cities there are often several government charges and levies involved. According to the Property Council of Australia¹⁹ approximately 25% of a new house price nationally is attributable to the impact of government costs in 2005. In North West Sydney the proportion was 35%, whilst in South West Sydney it was 31%. Critics of such charges argue that house prices would be much lower without them. They advocate that such charges should be absorbed by the state and local governments themselves. Advocates of such charges though, propose that these charges are reasonable as long as they reflect the true marginal cost to society of building new homes on the periphery of the capital cities. In effect, by absorbing such costs the state government is subsidising capital city growth beyond the socially optimal boundaries. This would in turn create a higher than socially optimal level of population, traffic, pollution, etc.

There are two opposing views on the impact of releasing more land on the periphery of capital cities. Firstly, the view that the impact will be relatively small, such as espoused by Rory Robertson of Macquarie Bank:

*"There will be downward pressure on houses near the fringes, but I don't think it will be anything substantial in terms of reduction in city wide home prices, in city average home prices."*²⁰

And, the view espoused by Alan Moran (Institute of Public Affairs):

*"... There's clearly a relationship between houses on the periphery and houses in the centre. The periphery is the thing that dictates the price generally."*²¹

¹⁹ Property Council of Australia, "Reasons to be fearful? Government taxes, charges and compliance costs and their impact on housing affordability", summary report – residential development costs benchmarking study, March 2006

²⁰ Bevan, S., "Home Ownership a distant dream for many", The 7.30 report, Australian Broadcasting Corporation, Broadcast on 6/2/2007 – <http://www.abc.net.au/7.30/content/2007/s1841718.htm>

It is not clear whether households on the margin of the housing market would prefer to live on the edges of Australia's large capital cities. This is because it is relatively distant to the majority of jobs, further away from social networks (such as friends and family), and can be expensive due to development charges by the state and local governments.

Which one of these views is correct is difficult to ascertain, however the general consensus among economists appears to favour that of Rory Robertson.

As will be demonstrated in a later part of this submission, the number of housing finance commitments for the construction of new dwellings has been relatively low over the past few years. This represents a relatively low level of additions to the supply of new housing coming into the market. It is particularly curious at a time of relatively high demand for housing.

Housing price fundamentals

According to the OECD²², the Australian house price to rent ratio was noticeably higher than its "fundamental" levels in 2004. It was approximately 75% higher than its 35 year average. Comparatively, the Australian house price to income ratio stood at about 50% above its 35 year average.

Geographical distribution of housing affordability

The housing affordability measures discussed so far have been for the average, or median, household across Australia. They do not take into account the geographical distribution of housing affordability.

In terms of geography, the HIA Housing Affordability Index indicates that the level of housing affordability in Capital Cities has been lower than that for 'Other areas' for at least between the December quarter 2001 and the December quarter 2007²³. This is perhaps unsurprising given that capital cities contain most of the high paid jobs and have a scarcity of available land for housing. Over this same period though, the level of housing affordability for both capital cities and 'other areas' has fallen, within the gap in index points being relatively lower in the December quarter 2007 compared with the December quarter 2001.

²¹ Bevan, S., "Home Ownership a distant dream for many", The 7.30 report, Australian Broadcasting Corporation, Broadcast on 6/2/2007 – <http://www.abc.net.au/7.30/content/2007/s1841718.htm>

²² OECD, OECD Economic Outlook, Issue 2, 2005, p.135

²³ Housing Industry Association, "Supply Measures will improve affordability", media release, 12/2/2008

According to the 2006 Census of Population and Housing, the number of dwellings that were fully owned in Australia fell from 2,657,971 in 1996 to 2,478,265 (a fall of 179,706 or 6.8%). Comparatively, the number of dwellings being purchased increased from 1,656,062 in 1996 to 2,448,211 in 2006 (an increase of 792,149 or 48%). The number of dwellings being rented increased from 1,865,961 in 1996 to 2,063,945 in 2006 (an increase of 197,984 or 11%). What this means, is that there has been a shift away from dwellings being fully owned towards dwellings being purchased and those being rented.

Data based on the 2006 Census of Population and Housing show that the median household income per week in 1996 was \$619 and in 2006 was \$1,025 (in nominal dollars); the median housing loan repayment per month in 1996 was \$780 in 1996 (or \$180 per week if we multiply by 12, divide by 365 days in a year, and then multiply by 7 days in a week) and \$1,300 in 2006 (or \$299 per week if we multiply by 12, divide by 365 days in a year, and then multiply by 7 days in a week); and, the median rent per week was \$123 in 1996 and \$191 in 2006 – see Table 1.

Table 1: National Median household and dwelling indicators from the 2006 Census of Population and Housing for Australia

	1996	2001	2006
Median household income (\$ / week)	619	786	1,025
Median housing loan repayment (\$ / month)	780	867	1,300
Median rent (\$ / week)	123	145	191

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

Table 2, shows some crude measures of national housing affordability based on data in Table 1.

Table 2: National Median household indicators of housing affordability from the 2006 Census of Population and Housing for Australia

	1996	2001	2006
Median housing loan repayment to median household income ratio	0.29	0.25	0.29
Median rent to median household income ratio	0.20	0.18	0.19

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

Based on these crude measures of housing affordability, the ratio of housing loan repayment to median household income in Australia fell from 0.29 in 1996 to 0.25 in 2001 (i.e. an increase in housing affordability), before increasing back to 0.29 in 2006.

For national rental affordability, the median rent to median household income ratio fell from 0.20 in 1996 to 0.18 in 2001 (i.e. an increase in rental affordability), before increasing to 0.19 in 2006. But, there are different geographical incidences of housing affordability based on the Census of Housing and Population data, as shown in Table 11 and Table 12.

For house purchase affordability by state, the ratio of median housing loan repayment to median household income ratio compared with its national equivalent was higher in New South Wales (by 2.3 percentage points) and Queensland (by 1.8 percentage points) in 1996. The difference between the New South Wales ratio and the national average ratio increased from 1996 to 2001 (from 2.3 percentage points above to 4.5 percentage points above), and marginally from 2001 to 2006 (from 4.5 percentage points above to 4.6 percentage points above). Comparatively, the difference between the Queensland ratio and the national average fell from 1996 to 2001 (from 1.8 percentage points above to 1.3 percentage points above), and fell again from 2001 to 2006 (from 1.3 percentage points above to 0.2 of a percentage point below). All other states recorded a median housing loan repayment to median household income ratio below the national average in 1996, 2001, and 2006.

Table 3: Level of Median housing loan repayment to median household income ratio - comparison with national average by state (percentage points difference)

	1996	2001	2006
New South Wales	2.3	4.5	4.6
Victoria	-2.0	-0.8	-0.9
Queensland	1.8	1.3	-0.2
South Australia	-1.2	-3.4	-2.7
Western Australia	-2.1	-0.1	-2.9
Tasmania	-3.0	-3.7	-4.2

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

For renting affordability by state, the ratio of median rent to median household income ratio compared with the national average was higher in New South Wales (by 2.1 percentage points) and Queensland (by 1.1 percentage points) in 1996. For New South Wales, the ratio relative to the national average was unchanged from 1996 to 2001 (2.1 percentage points above the national average), but fell from 2001 to 2006 (from 2.1 percentage points above the national average to 1.7 percentage points above the national average). For Queensland, the ratio relative to the national average fell from 1996 to 2001 (from 1.1 percentage points above the national average to 0.9 of a percentage point above the national average), and fell marginally from 2001 to 2006 (from 0.9 of a percentage point above the national average to 0.8 of a percentage point above the national average).

Table 4: Level of Median rent to median household income ratio – comparison with national average by state (percentage points difference)

	1996	2001	2006
New South Wales	2.1	2.1	1.7
Victoria	-0.8	0.0	-0.5
Queensland	1.1	0.9	0.8
South Australia	-3.2	-2.8	-1.7
Western Australia	-2.5	-1.9	-2.6
Tasmania	-2.5	-2.9	-1.8

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

By capital city, the extremes of housing affordability become much clearer. This is particularly so for the Sydney statistical division, with the median housing loan repayment to median household income ratio in 1996 being 1.8 percentage points higher than the national average, rising to 3.0 percentage points higher in 2001, and 6.7 percentage points higher in 2006.

Table 5: Level of Median housing loan repayment to median household income ratio – comparison with national average by state capital city statistical division (percentage points difference)

	1996	2001	2006
Sydney	1.8	3.0	6.7
Melbourne	-2.2	-2.1	-1.4
Brisbane	0.2	-1.3	-2.3
Adelaide	-2.3	-3.1	-2.2
Perth	-1.9	-0.6	-1.6
Greater Hobart	-3.9	-3.8	-4.3

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

For renting affordability, the Sydney statistical division recorded a median rent to median household income ratio that was 2.2 percentage points higher than the national average in 1996, rising to 2.8 percentage points higher in 2001, and 3.0 percentage points higher in 2006. The Brisbane statistical division was the only other capital city to consistently have its median rent to median household income ratio above the national average over this period, with the difference being 0.6 of a percentage point in 1996, 0.2 of a percentage point in 2001, and 1.2 percentage points in 2006.

Table 6: Level of Median rent to median household income ratio – comparison with national average by state capital city statistical division (percentage points difference)

	1996	2001	2006
Sydney	2.2	2.8	3.0
Melbourne	-0.9	0.1	-0.1
Brisbane	0.6	0.2	1.2
Adelaide	-2.0	-1.8	-0.7
Perth	-1.2	-1.1	-2.0
Greater Hobart	-2.3	-2.6	-2.0

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

For housing affordability, in 2006 the ratio of median housing loan repayment to median household income was higher than its state average for the statistical divisions of Sydney (2.2 percentage points higher than New South Wales's ratio), Perth (1.3 percentage points higher than Western Australia's ratio), and Adelaide (0.6 of a percentage point higher than South Australia's ratio). It was lower in the Statistical Divisions of Brisbane (2.1 percentage points lower than Queensland's ratio), Melbourne (0.5 of a percentage point lower than Victoria's ratio), and Greater Hobart (0.1 of a percentage point lower than Tasmania's ratio) – see Table 7.

Table 7: Level of Median housing loan repayment to median household income ratio – comparison with state average by state capital city statistical division (percentage points difference)

	1996	2001	2006
Sydney	-0.5	-1.5	2.2
Melbourne	-0.2	-1.2	-0.5
Brisbane	-1.6	-2.6	-2.1
Adelaide	-1.0	0.3	0.6
Perth	0.2	-0.5	1.3
Greater Hobart	-0.9	-0.2	-0.1

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

For rental affordability, in 2006 the ratio of median rent to median household income was higher than its state average in the statistical divisions of Sydney (1.4 percentage points higher than New South Wales's ratio), Adelaide (0.9 of a percentage point higher than South Australia's ratio), Perth (0.6 of a percentage point higher than Western Australia's ratio), Melbourne (0.4 of a percentage point higher than Victoria's ratio), and Brisbane (0.4 of a percentage point higher than Queensland's ratio). It was only lower in the Greater Hobart Statistical Division (0.3 of a percentage point lower than Tasmania's ratio) – Table 8.

Table 8: Level of Median rent to median household income ratio – comparison with state average by state capital city statistical division (percentage points difference)

	1996	2001	2006
Sydney	0.1	0.7	1.4
Melbourne	-0.2	0.1	0.4
Brisbane	-0.5	-0.7	0.4
Adelaide	1.2	1.0	0.9
Perth	1.3	0.8	0.6
Greater Hobart	0.2	0.3	-0.3

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

Sydney

Because of the relatively high level of median housing loan repayment to median household income ratio compared with national average and the median rent to median household income ratio compared with the national average, the statistical subdivisions of the Sydney statistical division will be examined in the following section – see Table 9.

For Housing affordability, Table 9 shows that the median housing ratio to median household income ratio compared with the national average in the Sydney statistical division is geographically uneven. In 2006, the statistical sub divisions where this ratio was higher than for the statistical division as a whole were Canterbury-Bankstown (13.1 percentage points higher than the national average), Gosford-Wyong (11.2 percentage points higher than the national average), Inner Sydney (10.6 percentage points higher than the national average), Central Western Sydney (9.6 percentage points higher than the national average), Fairfield-Liverpool (8.4 percentage points higher than the national average), St George Sutherland (8.1 percentage points higher than the national average) and the Eastern Suburbs (6.8 percentage points higher than the national average). Those statistical subdivisions where the ratio was lower than for the statistical division as a whole in 2006 were Central Northern Sydney (1.0 percentage point lower than the national average), Outer Western Sydney (2.1 percentage points higher than the national average), Lower Northern Sydney (3.0 percentage points higher than the national average), Outer South Western Sydney (3.3 percentage points higher than the national average), Northern Beaches (5.1 percentage points higher than the national average), and Blacktown (6.5 percentage points higher than the national average). For the Central Northern Sydney statistical subdivision in 2006, the ratio of median housing loan repayment to median household income ratio was actually lower than the national average in 1996 (by 3.5 percentage points), 2001 (by 1.2 percentage points) and 2006 (by 1.0 percentage point).

Table 9: Level of Median housing loan repayment to median household income ratio - comparison with national average by statistical subdivisions in the Sydney statistical division (percentage points difference)

	1996	2001	2006
Blacktown	0.7	1.6	6.5
Canterbury-Bankstown	6.6	9.5	13.1
Central Northern Sydney	-3.5	-1.2	-1.0
Central Western Sydney	4.3	5.4	9.6
Eastern Suburbs	5.9	9.6	6.8
Fairfield-Liverpool	3.0	4.8	8.4
Gosford-Wyong	9.4	7.1	11.2
Inner Sydney	10.6	9.1	10.6
Inner Western Sydney	6.0	8.3	9.5
Lower Northern Sydney	3.1	6.1	3.0
Northern Beaches	2.6	6.2	5.1
Outer South Western Sydney	-1.2	0.5	3.3
Outer Western Sydney	-2.5	0.1	2.1
St George-Sutherland	2.4	3.7	8.1
Sydney	1.8	3.0	6.7

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

For rental affordability, the median rent to median household income ratio compared with the national average in the Sydney statistical division is also geographically uneven. In 2006, the statistical sub divisions where this ratio was higher than for the statistical division as a whole were Inner Sydney (6.1 percentage points higher than the national average), Inner Western Sydney (5.3 percentage points higher than the national average), Eastern Suburbs (4.8 percentage points higher than the national average), Gosford-Wyong (4.8 percentage points higher than the national average), Northern Beaches (4.7 percentage points higher than the national average), Central Western Sydney (4.2 percentage points higher than the national average), Canterbury-Bankstown (4.0 percentage points higher than the national average), and St George-Sutherland (3.5 percentage points higher than the national average). Those statistical subdivisions where the ratio was lower than for the statistical division as whole in 2006 were Outer South Western Sydney (1.4 percentage points lower than the national average), Blacktown (0.5 of a percentage point lower than the national average), Outer Western Sydney (0.1 of a percentage point lower than the national average), Central Northern Sydney (equal to the national average), Fairfield-Liverpool (0.1 of a percentage point higher than the national average), and Lower Northern Sydney (2.0 percentage points higher than the national average). The ratio of median rent to median household income was lower than the national average in the sub divisions of Outer South Western Sydney

(1.4 percentage points lower) in 2006, Blacktown (0.5 of a percentage point lower), and Outer Western Sydney (0.1 of a percentage point lower) – see Table 10.

Table 10: Level of Median rent to median household income ratio - comparison with national average by statistical subdivisions in the Sydney statistical division (percentage points difference)

	1996	2001	2006
Blacktown	-0.5	-0.1	-0.5
Canterbury-Bankstown	3.7	4.2	4.0
Central Northern Sydney	0.5	1.6	0.0
Central Western Sydney	3.7	4.6	4.2
Eastern Suburbs	6.7	8.6	4.8
Fairfield-Liverpool	-0.2	0.0	0.1
Gosford-Wyong	7.1	5.6	4.8
Inner Sydney	4.8	6.3	6.1
Inner Western Sydney	4.4	5.4	5.3
Lower Northern Sydney	4.1	6.0	2.0
Northern Beaches	3.0	6.4	4.7
Outer South Western Sydney	-2.1	-1.8	-1.4
Outer Western Sydney	-0.0	-0.2	-0.1
St George-Sutherland	2.8	3.5	3.5
Sydney	2.2	2.8	3.0

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

The previous two tables show that there are parts of the Sydney statistical division where housing affordability is relatively reasonable compared with the national average. However, for some parts of the Sydney statistical division the differences in housing affordability with the national average are relatively large.

Housing stress

Housing stress can be defined in many ways. The most traditional measure was the Ontario measure. This is a widely used international benchmark that ascertains eligibility of a household for housing assistance under social housing programs. That benchmark is set where the proportion of gross household income spent on housing exceeds 30% for those households in the bottom 40 percentiles on the household income distribution. While this benchmark is typically used in Australia to assess the eligibility of a low income household for access to the waiting list for public housing and/or for rent assistance, it is not the measures used in housing affordability index measures that are widely reported in the media.

According to the latest Reserve Bank of Australia's *Financial Stability Review* (March 2008), housing loan arrears nationally remain at levels that are low by both historical and international standards. The ratio of non-performing housing loans to total housing loans on bank's domestic books was 0.32% as at the end of December 2007, which was unchanged from a year earlier. The national 90-day arrears rate for housing loans was also broadly unchanged over 2007, at 0.4% in December. For low documentation loans, the 90-arrears rate was 0.7% in November 2007 – more than double for prime full-documentation loans, but still largely unchanged from a year earlier. Comparatively, the arrears rate for non-conforming loans (borrowers with a poor credit history), has risen significantly and now stands at 7.25%. But these loans represent less than 1% of all outstanding housing loans in Australia.

According to the Reserve Bank of Australia's *Financial Stability Review* (March 2008), although the aggregate data continue to suggest that household finances are in sound shape, housing loan arrears are higher in New South Wales than in other states. This is particularly so for Western Sydney where economic conditions have been relatively weak and house prices have been falling and led to a rise in arrears rates between 2003 and 2006. Comparatively, arrears rates in a number of other parts of Sydney have remained relatively stable over this period.

While the ratio of repossession applications to dwelling stock in New South Wales is more than double that of the 1990's, the Reserve Bank of Australia (in its *Financial Stability Review*, March 2008) partially attributes this to a change in the relationship between the variables and the emergence of non-ADI lenders that are more likely to seek repossession.

In summary, current evidence of housing stress based on a number of measures is not showing substantial housing stress nationally. Nonetheless, there do appear to be pockets of housing stress, particularly in Western Sydney.

Housing Finance Data and First Home Buyers

For buyers of housing in the current housing market of relatively low affordability it is a difficult time to enter.

Buyers of dwellings can be either investors or owner occupiers. The share of the national value of housing finance for owner occupation purposes was 69% in the year to February 2008 (down from 84% in the year to February 1993)²⁴. Comparatively, the share of the national value of housing finance for investment

²⁴ ABS, cat. no.: 5609.0 - Housing Finance, Australia, Feb 2008, Table 11. HOUSING FINANCE COMMITMENTS (Owner Occupation and Investment Housing), By Purpose: Australia, (\$'000)

housing purposes was 31% in the year to February 2008 (up from 16% in the year to February 1993). This data tells us that the share of investors purchasing dwellings has increased over the past 15 years.

Based on housing finance data from the Australian Bureau of Statistics²⁵, The number of new dwellings constructed in the year to February 2008 was 56,439 nationally. This is lower than the average of 65,899 dwellings constructed over the past 20 years—and the number of new dwellings constructed has been lower than the 20 year average since the year to February 2003. In the year to February 2008 there were 33,396 new dwellings purchased (compared with a 20 year average of 21,776), and 693,831 established dwellings were purchased (compared with a 20 year average of 426,155). These statistics highlight that there has been a relatively low level of dwellings constructed to supply the housing market.

According to the Australian Bureau of Statistics²⁶, the proportion of dwellings financed by First Home Buyers nationally was 17.4% in the year to February 2008. This is lower than the 15-year average of 19.4%.

In summary, over the past few years the proportion of investors purchasing housing has increased and the proportion of first home buyers has fallen. In addition, the share of the value of housing finance for investment purposes has risen over the past 15 years at the expense of owner occupation purposes, and a relatively low number of new dwellings are being constructed.

Conclusion

There is no simple and quick market-based solution to housing affordability. If a government did implement caps on house prices, there would probably be an even larger gap between the quantity of housing demand and the quantity of housing supplied. There would also be a deadweight loss to society (mainly due to a relatively lower producer surplus).

Probably the simplest and quickest methods of reducing housing affordability- but one which would have other system-wide deleterious and distributional inequity outcomes - would be a recession, higher interest rates, or higher unemployment²⁷. As the OECD noted in 2005:

²⁵ ABS, cat. no.: 5609.0 - Housing Finance, Australia, Feb 2008, Table 1. HOUSING FINANCE COMMITMENTS (Owner Occupation), By Purpose: Australia (Number, \$000)

²⁶ ABS, cat. no.: 5609.0 - Housing Finance, Australia, Feb 2008, TABLE 9a. HOUSING FINANCE COMMITMENTS (Owner Occupation), By Type of Buyer and Loan: Australia, Original

²⁷ Schneiders, B. and Millar, R., "Australian dream just a recession away", *The Age*, 17/2/2007

“if house prices were to adjust downward, possibly in response to an increase in interest rates or for other reasons, the historical record suggests the drops (in real terms) might be large, and that the process could be protracted”

This large fall in house prices would certainly exceed any fall in household incomes, thus resulting in a lower house price / income ratio, and so housing affordability. Based on long run housing price fundamentals, the shift appears to be more a question of when rather than if housing affordability will improve.

In socio-economic terms, it is no surprise to hear relatively more stories of low income households being forced into default on their home loans. This is exactly what one would expect at, or near, the top of an economic cycle which is characterised by relatively high interest rates and high house prices. This probably explains why areas of relatively low socio-economic status, such as Western Sydney, tend to be affected the most during these periods.

Governments can, however, take actions to marginally address housing affordability. State governments and local governments could increase the amount of land available, which would increase the supply of housing over the medium term, and result in lower house prices than would otherwise have been the case.

Some aspects of housing affordability may never change. Geography will probably still play a large part in determining the demand for housing. Cities/towns and suburbs in capital cities which face relatively high house prices tend to be either close to the CBD or along the coast of Australia. In these areas, it is not easy to match the high demand for more supply for land. Thus, low housing affordability is geographically concentrated because simply these areas are where people prefer to live.

While geography may be part of the problem for housing affordability, as Rory Robertson points out²⁸, geography may play a part in a long run easing of housing affordability. If governments actively decentralised their activities and improved transportation and infrastructure, then demand for land and houses in capital cities would be reduced.

²⁸ Robertson, R., “No politician can afford to fix housing affordability”, The Sydney Morning Herald, 18/10/2007

Appendix

Table 11: Median household indicators from the 2006 Census of Population and Housing for Australian states (by place of enumeration count method)

	1996	2001	2006
New South Wales			
Median household income (\$ / week)	637	826	1,034
Median housing loan repayment (\$ / month)	867	1,073	1,517
Median rent (\$ / week)	140	170	210
Victoria			
Median household income (\$ / week)	628	812	1,021
Median housing loan repayment (\$ / month)	780	867	1,300
Median rent (\$ / week)	123	145	191
Queensland			
Median household income (\$ / week)	597	749	1,031
Median housing loan repayment (\$ / month)	800	867	1,300
Median rent (\$ / week)	125	145	200
South Australia			
Median household income (\$ / week)	539	703	885
Median housing loan repayment (\$ / month)	650	671	1,018
Median rent (\$ / week)	90	110	150
Western Australia			
Median household income (\$ / week)	635	784	1,063
Median housing loan repayment (\$ / month)	743	862	1,213
Median rent (\$ / week)	110	130	170
Tasmania			
Median household income (\$ / week)	518	643	800
Median housing loan repayment (\$ / month)	585	607	867
Median rent (\$ / week)	90	100	135

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

Table 12: Median household indicators of housing affordability from the 2006 Census of Population and Housing for Australian states (by place of enumeration count method)

	1996	2001	2006
New South Wales			
Median housing loan repayment to median household income ratio	0.31	0.30	0.34
Median rent to median household income ratio	0.22	0.21	0.20
Victoria			
Median housing loan repayment to median household income ratio	0.29	0.25	0.29
Median rent to median household income ratio	0.20	0.18	0.19
Queensland			
Median housing loan repayment to median household income ratio	0.31	0.27	0.29
Median rent to median household income ratio	0.21	0.19	0.19
South Australia			
Median housing loan repayment to median household income ratio	0.28	0.22	0.26
Median rent to median household income ratio	0.17	0.16	0.17
Western Australia			
Median housing loan repayment to median household income ratio	0.27	0.25	0.26
Median rent to median household income ratio	0.17	0.17	0.16
Tasmania			
Median housing loan repayment to median household income ratio	0.26	0.22	0.25
Median rent to median household income ratio	0.17	0.16	0.17

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

Table 13: Median household indicators from the 2006 Census of Population and Housing for capital city statistical divisions of Australian states (by place of enumeration count method)

	1996	2001	2006
Sydney			
Median household income (\$ / week)	747	988	1,153
Median housing loan repayment (\$ / month)	1,000	1,219	1,800
Median rent (\$ / week)	165	210	250
Melbourne			
Median household income (\$ / week)	686	888	1,078
Median housing loan repayment (\$ / month)	800	900	1,300
Median rent (\$ / week)	130	165	200
Brisbane			
Median household income (\$ / week)	661	829	1,111
Median housing loan repayment (\$ / month)	840	867	1,300
Median rent (\$ / week)	135	155	220
Adelaide			
Median household income (\$ / week)	560	722	922
Median housing loan repayment (\$ / month)	650	700	1,083
Median rent (\$ / week)	100	120	165
Perth			
Median household income (\$ / week)	643	805	1,085
Median housing loan repayment (\$ / month)	758	867	1,300
Median rent (\$ / week)	120	140	180
Greater Hobart			
Median household income (\$ / week)	569	694	903
Median housing loan repayment (\$ / month)	620	650	975
Median rent (\$ / week)	100	110	150

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)

Table 14: Median household indicators of housing affordability from the 2006 Census of Population and Housing for capital city statistical divisions of Australian states (by place of enumeration count method)

	1996	2001	2006
Sydney			
Median housing loan repayment to median household income ratio	0.31	0.28	0.36
Median rent to median household income ratio	0.22	0.21	0.22
Melbourne			
Median housing loan repayment to median household income ratio	0.27	0.23	0.28
Median rent to median household income ratio	0.19	0.19	0.19
Brisbane			
Median housing loan repayment to median household income ratio	0.29	0.24	0.27
Median rent to median household income ratio	0.20	0.19	0.20
Adelaide			
Median housing loan repayment to median household income ratio	0.27	0.22	0.27
Median rent to median household income ratio	0.18	0.17	0.18
Perth			
Median housing loan repayment to median household income ratio	0.27	0.25	0.28
Median rent to median household income ratio	0.19	0.17	0.17
Greater Hobart			
Median housing loan repayment to median household income ratio	0.25	0.22	0.25
Median rent to median household income ratio	0.18	0.16	0.17

Source: ABS, 2006 Census of Population and Housing; Time Series Profile, T02 Selected Averages and medians for time series (by place of enumeration count method)