



First Home Buyers: The Big Picture

April 2014

Key Points:

- There has been considerable coverage of late regarding the First Home Buyer (FHB) market share, with the widespread perception that this group is being 'squeezed out' by investors.
- In reality, FHB activity rates are explained by a more complex set of circumstances. These include drag-forward effects, the age structure of the population, labour market weaknesses, non-mortgage financed FHB purchases, and more caution by FHBs in terms of entering the recovering market.
- In terms of supporting FHB participation, the policy emphasis must be on delivering a greater flow of affordable housing supply.
- Policy measures aimed at dissuading investor participation must be avoided, which could hurt building activity and lead to deteriorating rental affordability.

Concerns about First Home Buyer (FHB) participation in the home purchase market have surfaced repeatedly in the media over the past year. This has been largely based on ABS Housing Finance figures showing that the FHB share of the owner occupier market reached a low of 12.3 per cent during November 2013. This was the lowest share recorded since compilation of the series began in July 1991, and is based on mortgage lending volumes.

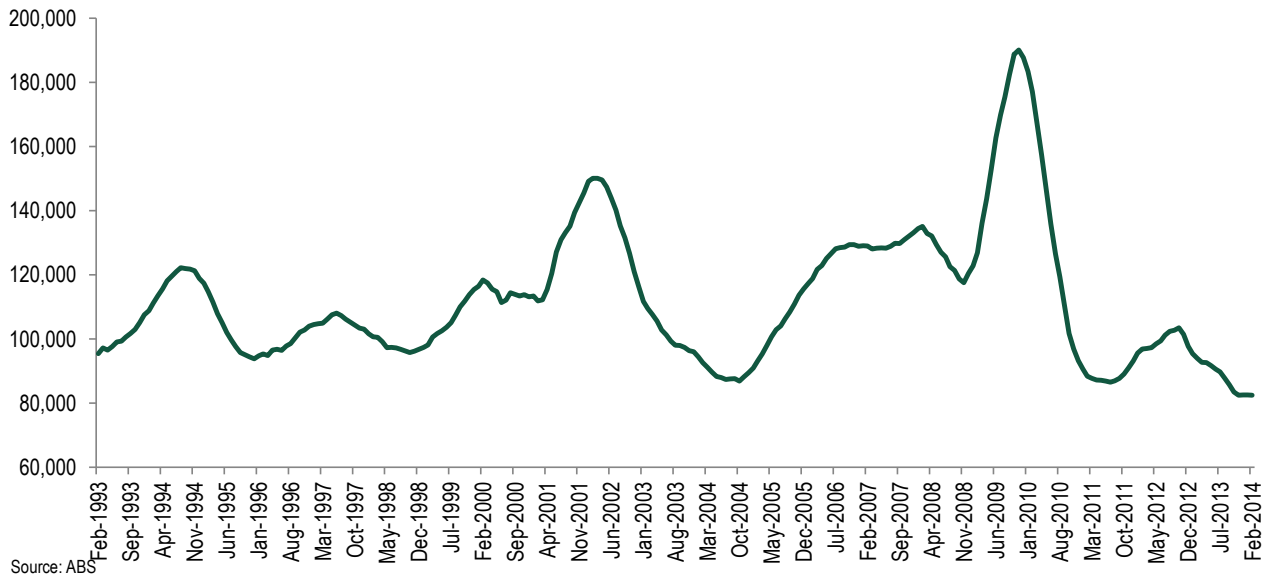
Commentary around the low FHB share has typically invoked the narrative that younger buyers are being 'squeezed out' of the market by investors with deeper pockets. The pick-up in home price growth and solid rental yields is attributed as being the main factor behind stronger investor interest in the market.

Low FHB shares have also been attributed to changes in FHB grant regimes in many states, which have seen the grant for the purchase of existing homes being reduced or eliminated entirely. This has been accompanied by substantially increased FHOGs for the acquisition of new homes.

Developments in the number of FHB mortgages are illustrated below for the period between 1993 and 2014. The then federal government's stimulus programme during 2008-09 provided strong incentives for FHB purchase and as a result, FHB activity surged. The peak occurred during the year to November 2009, with about 190,000 FHB mortgages being issued to owner occupiers. The FHB share of the owner occupier market peaked at 29 per cent during this period.

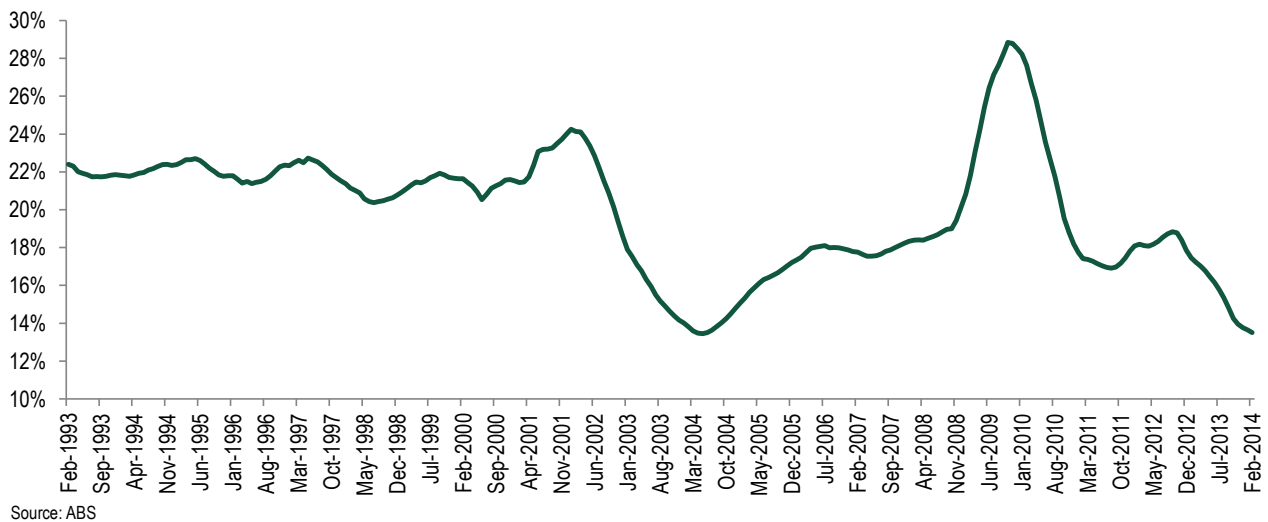


Number of Owner Occupier Loans to FHBs (Moving Annual Total), 1993 to 2014



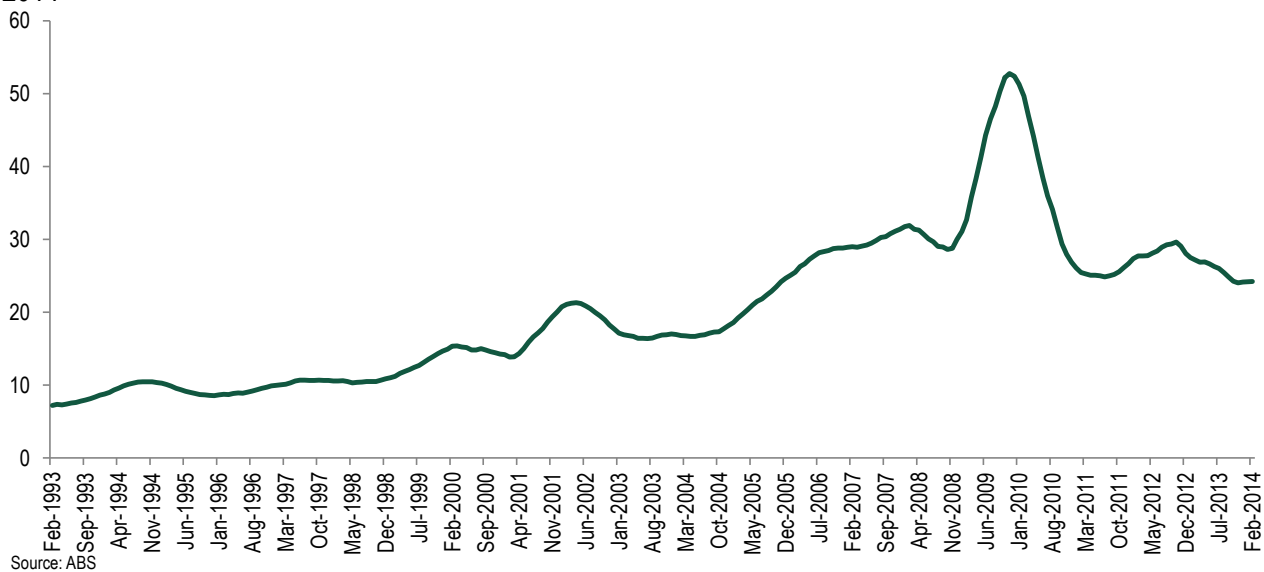
In the year to January 2014, about 82,500 loans to FHBs were issued, representing a 13.6 per cent share of the owner occupier market during this period. Developments in the FHB market share are shown below for the 1993 to 2014 period.

Number of FHB Loans as a percentage of Total Owner Occupier Loans (Moving Annual Total), 1993 to 2014



The chart below provides an overview of the value of loans paid to FHBs between 1993 and 2014 for owner occupier purposes. The value of FHB loans peaked at about \$53 billion in the year to November 2009 during the government stimulus post-GFC. In the twelve months to January 2014, the total value of FHB loans was \$24.2 billion.

Total Value of Owner Occupier FHB Loans (Moving Annual Total - \$ billions), 1993 to 2014



This paper examines the entire set of factors affecting FHB participation in the market and finds the story is more complex than media coverage suggests. There are quite a number of explanations behind the current volume of FHB activity. These include:

- Drag-forward effects
- Age structure of the population
- Labour market weakness
- FHB investors
- Non-mortgage FHB purchases
- Slower FHB response to strengthening market

Each of these factors are discussed in turn over the next few paragraphs.

Drag-forward Effects

Following the onset of the GFC during 2008, a large government stimulus was initiated in order to support demand in the economy. There was a range of measures targeting home purchase incentives. Some examples are:-

- The Commonwealth Government's First Home Owner Grant 'Boost' was in effect from October 2008 to September 2009. The FHOGB was increased to \$21,000 for new homes and to \$14,000 for existing homes during this period.
- Following the withdrawal of the FHOGB Boost in December 2010, the Victorian state government introduced an augmented FHOGB from July 2010 to June 2012. In regional areas, the total FHOGB for new homes was \$26,500, while in metropolitan areas, the total was \$20,000. For existing homes the standard \$7,000 grant was still applicable in both regional and metropolitan areas.
- In NSW, a stamp duty exemption for FHBs purchasing new homes valued at less than \$500,000 was introduced in January 2012, with a concessional rate of stamp duty applied to houses valued between \$500,000 and \$650,000.

These incentives resulted in a large number of first home buyers entering the market earlier than they would otherwise have done. As a result, there were fewer FHBs left to purchase in the following few years.

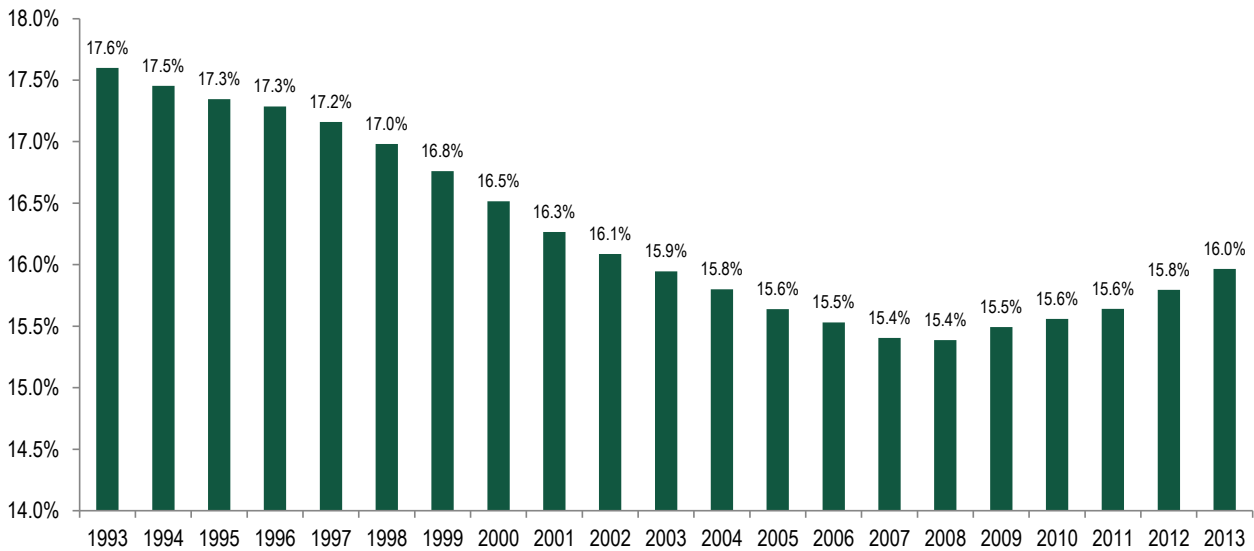
Thus, we can say that FHB purchases were skewed forward by the grants and concessions on offer during and following the GFC. The fact that FHB activity over the past five years has not been hugely different to its long term average is consistent with this characterisation. Between February 2008 and January 2014, there were around 112,000 FHB mortgages issued per year. This is only a little lower than the 115,400 per year issued over the preceding decade. This supports the view that FHB activity is not in long term decline, with its pattern having simply been skewed by variations in grant incentives post-GFC.

Age structure of the population

FHBs are generally concentrated within certain age groups and changes in the composition of the population accordingly have a strong influence on FHB activity. The chart below shows how the key FHB age group (aged between 25 and 35 years) has been in long term decline as a share of the population, falling from 17.6 per cent in 1993 to 15.4 per cent in 2008. It is likely that this has partly contributed to the lower share of FHB activity in recent years.

Over the last five years, the 25 to 35 year age group’s share of the population has started to increase again. This will eventually cause the FHB segment of the market to become more active.

Share of Population in the 25 to 35 Year Age Group, 1993 to 2013



Source: ABS

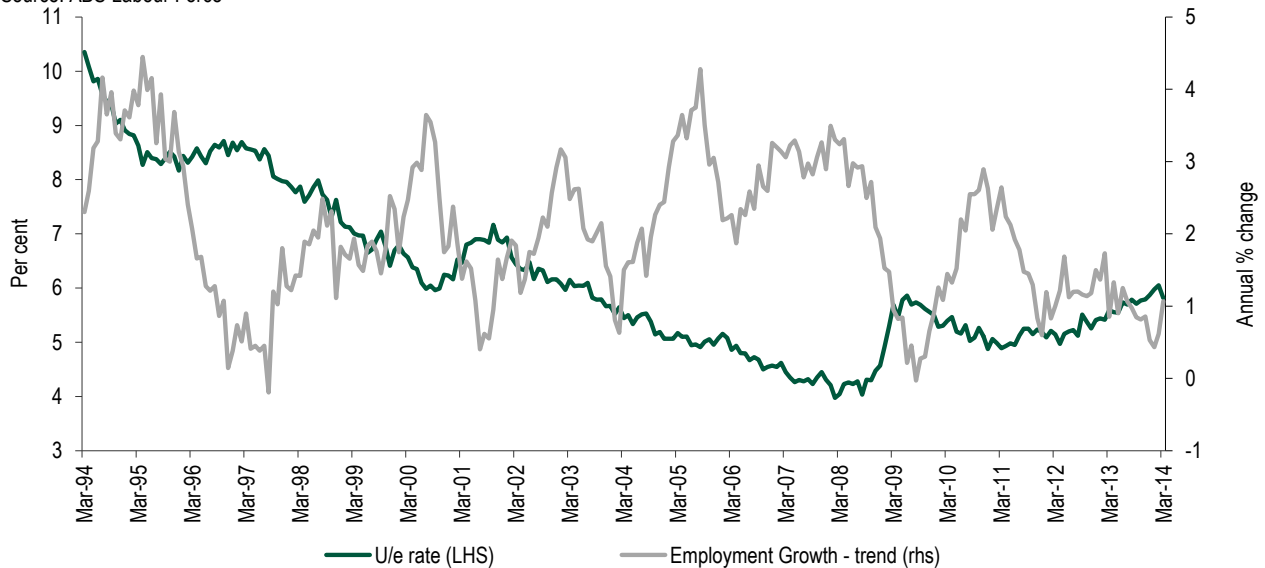
Labour market weakness

Over the past two years, the unemployment rate has increased from 5.0 per cent to decade high of 6.0 per cent in February 2014 (and then declined to 5.8 per cent in March). At the same time, the rate of employment growth fell below 1 per cent for the first time since the depths of the GFC. This is illustrated in the chart below. It is also worth noting that the profile of employment creation is weak, with part-time rather than full-time employment accounting for the lion’s share of jobs growth over the past year.

Younger employees tend to bear the brunt of weak labour markets, with youth unemployment rates usually significantly higher than the rate for the general population. As the FHB market is dominated by younger home buyers, their participation in the home purchase market will be disproportionately affected by a weaker labour market, risks to incomes and any uncertainty around employment prospects. This is because potential FHBs will be less willing to enter the market when such risks are present. The ability of would-be FHBs to receive mortgage financing will also be seriously curtailed in a scenario of lower employment rates and downside risks to incomes. Accordingly, it is likely that the weakening labour market is playing a significant role in depressing FHB activity.

Australia's Labour Market

Source: ABS Labour Force



FHB Investors

The role of strong rental growth, record low interest rates and accelerating prices in attracting investors to the market has been well documented. There is some evidence that these conditions have resulted in some buyers acquiring their first home as an investment rather than buying for their own occupation. These buyers then continue to rent or to live with family members. Consequently, such buyers do not show up in the official FHB data and the actual number of FHB transactions is understated as a result.

Non-mortgage FHB purchases

As the official ABS data on FHBs only include mortgaged-financed home purchases for owner occupation, FHB purchases made without resorting to debt financing will not show up on the statistical radar. Such purchases could be financed by savings, inheritances, informal funding from family/friends, insurance payouts, legal compensation or other sources. There is anecdotal evidence that the importance of financial support from parents in financing FHB purchase has increased.

As the population ages, the number of deaths per year in Australia is increasing steadily (from about 131,000 in 2005 to 147,000 in 2012). This means that the number of people per year in receipt of inheritances is rising, potentially enabling more non-debt financed home acquisitions by FHBs. This could be another source of understatement in the official FHB figures.

Slower FHB response to strengthening market

Australia's housing market turned the corner during 2013. New dwelling construction increased for the first time in three years and home price growth accelerated. This was against the backdrop of healthy rental yields and record-low interest rates.

In a recovering market, more seasoned buyers like investors and non-FHBs are likely to be the fastest to respond to the improved conditions. FHBs are a little more risk averse, and will be less comfortable about entering the market at first. This means that their share of the market will temporarily flag as the market negotiates its turning point. Over time, we can expect FHB activity to gradually increase as the market recovery becomes more established.

Conclusion

The low share of the owner occupier mortgage market accounted for by FHBs is a temporary phenomenon, and reflects a unique mix of factors. These include:

- A substantial amount of FHB demand was dragged forward due to improved grant incentives and concessions during and following the GFC;
- The proportion of Australia's population in the key FHB age group was in long term decline up until quite recently;
- Labour market conditions are currently having a disproportionately detrimental effect on FHB participation in the market;
- Increasing numbers of first homes are purchased as investment properties, and do not show up as FHB purchases;
- More significant parental support and increased numbers of inheritances are facilitating mortgage-free FHB purchases;
- FHBs are much slower to enter the improving market than non-FHBs and investors - their market share has temporarily dipped as a result.

Over time, we expect FHB activity in the market to increase. This is for the following reasons:

- The share of population in the 25 to 35 year age group is starting to increase again;
- FHB confidence will grow as the housing market recovery becomes more consolidated;
- The eventual improvement in labour market conditions will facilitate greater FHB market participation; and
- Strong price growth will lead to the accumulation of home equity – allowing increased parental support for home purchase by FHBs.

The public commentary around FHB market participation has frequently focused on introducing policy measures to dissuade investor activity in the market. Such measures distract from the fact that the housing supply response to strong population growth over the past decade has been insufficient. The most likely impact of imposing penalties on investors is that fewer homes will be built. Fewer investors in the market will force the rental market to tighten and hurt the disposable incomes of households in that area of the market.

Accordingly, the real challenge will be for policymakers to ensure that the recovery of FHB activity over the coming years will be met with a strong supply of affordable housing. Australia has the fastest growing population of any major developed economy and it is vital that policy allows for the provision of an adequate dwelling stock for a population undergoing such strong increase. Policy measures with respect to FHBs, however well intentioned, must ultimately be judged on their ability to support stronger flows of new dwelling supply and their effectiveness in promoting improved housing affordability for ordinary households.